Supreme Court, U.S.
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No. _____

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1995

FIRST NATIONAL BANK & TRUST, WIBAUX, MONTANA, and ITS STOCKHOLDERS, Thomas E. Towe Trust, Karen James Trust, Kristin Hartley Trust, Sara Horsfall Trust, Andrew C. Towe Trust, Grant Investments Fund, Irene Koch, and Dorothy Tow,

[redacted] **Petitioners,**

vs.

THE COMPTROLLER OF THE CURRENCY,

[redacted] **Respondent.**

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

APPENDIX TO PETITION FOR WRIT OF CERTIORARI

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BANK CONSERVATION ACT

Act of March 9, 1933 (Emergency Banking and Bank Conservation Act), Title II, 48 Stat. 2

SEC. 203(a) **APPOINTMENT.**---The Comptroller of the Currency may, without notice or prior hearing, appoint a conservator, which may be the Federal Deposit Insurance Corporation, to take possession and control of a bank whenever the Comptroller determines that one or more of the following circumstances exist:

(1) any one or more of the conditions for appointment of a receiver for the bank specified in the first section of the Act of June 20, 1876 (12 U.S.C. 191) are present;

(2) the bank is not likely to be able to meet the demands of its depositors or pay its obligations in the normal course of business;

(3) the bank in an unsafe or unsound condition to transact business, including having substantially insufficient capital or otherwise;

(4)(A) the bank has incurred or is likely to incur losses that will deplete all or substantially all of its capital, and

(B) there is no reasonable prospect for the bank's capital to be replenished without Federal assistance;

(5) there is a violation or violations of laws, rules, or regulations, or any unsafe or unsound practice or condition which is likely to cause insolvency or substantial dissipation of assets or earnings, or is likely to weaken the bank's condition or otherwise seriously prejudice the interests of its depositors;

(6) there is concealment of books, records, or assets of the bank, or refusal to submit books, papers, records, or affairs of the bank for inspection to any examiner or to any lawful agent of the Comptroller;

(7) there is a willful or continuing violation of an order enforceable against the bank under section 8(i) of the Federal Deposit Insurance Act; or

(8) the bank's board of directors consists of fewer than 5 members.

(b) **JUDICIAL REVIEW.---**

(1) In General.---Not later than 20 days after the initial appointment of a conservator pursuant to this section, the bank may bring an action in the United States district court for the judicial district in which the home office of such bank is located, or in the United States District Court for the District of Columbia, for an order requiring the Comptroller to terminate the appointment of the conservator, and the court, upon the merits, shall dismiss such action or shall direct the Comptroller to terminate the appointment of such conservator. The Comptroller's decision to appoint a conservator pursuant

to this section shall be set aside only if the court finds that such decision was arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law.

(2) **Stay.**---The conservator may request that any judicial action or proceeding to which the conservator or the bank is or may become a party to stayed for a period of up to 45 days after the appointment of the conservator. Upon petition, the court shall grant such stay as to all parties.

(3) **Actions and Orders.**---Except as otherwise provided in this subsection, no court may take any action regarding the removal of a conservator, or restrain, or affect the exercise of powers or functions of a conservator. A court, upon application by the Comptroller, shall have jurisdiction to enforce an order of the Comptroller relating to---

(A) the conservatorship and the bank in conservatorship, or

(B) restraining or affecting the exercise of powers or functions of a conservator.

(c) **Additional Grounds for Appointment.**---In addition to the foregoing provisions, the Comptroller may appoint a conservator for a bank if---

() the bank, by an affirmative vote of a majority of its board of directors or by an affirmative vote of a majority of its shareholders, consents to such

appointment, or

(2) the Federal Deposit Insurance Corporation terminates the bank's status as an insured bank.

The appointment of a conservator pursuant to this subsection shall not be subject to review.

(d) **Exclusive Authority.**---The Comptroller shall have exclusive power and jurisdiction to appoint a conservator for a bank. Whenever the Comptroller appoints a conservator for any bank, the Comptroller may appoint the Federal Deposit Insurance Corporation conservator for such bank. The Federal Deposit Insurance Corporation, as such conservator, shall have all the powers granted under the Federal Deposit Insurance Corporation Act, and (when not inconsistent therewith) any other rights, powers, and privileges possessed by conservators of banks under this Act and any other provision of law. The Comptroller may also appoint another person as conservator, who shall be subject to the provisions of this Act.

(e) **Replacement of Conservator.**---The Comptroller may, without notice or hearing, replace a conservator with another conservator. Such replacement shall not affect the bank's right under subsection (b) to obtain judicial review of the Comptroller's original decision to appoint a conservator.

[Sec. 203 as amended by Act of August 9, 1989 (Financial Institutions Reform, Recovery, and

Enforcement Act of 1989, Sec. 802, Public Law 101-73, 103 Stat. 183; Act of December 19, 1991 (Federal Deposit Insurance Corporation Improvement Act of 1991), Sec. 13(c), Public Law 102-242, 105 Stat. 2271; 12 U.S. Code 203.]

§ 203(a) was amended December 19, 1992.

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MONTANA
BILLINGS DIVISION

FIRST NATIONAL BANK & TRUST, WIBAUX, MONTANA, and ITS STOCKHOLDERS, Thomas E. Towe Trust, Karen James Trust, Kristin Hartley Trust, Sara Horsfall Trust, Andrew C. Towe Trust, Grant Investments, Fund, Irene Koch, and Dorothy Tow,	) Cause No. CV 92-121-BLG-RWA) Judge Jack D. Shanstrom
Plaintiffs,	) **ORDER**
vs.	
THE COMPTROLLER OF THE CURRENCY,	
Defendant.	

Plaintiffs in the above-captioned cause have filed a request for a "post seizure constitutional hearing." Upon careful consideration of the briefs and documents submitted, I am prepared to rule.

BACKGROUND

On June 25, 1992, the Comptroller of the currency ("Comptroller") appointed a conservator to take possession and control of First National Bank and Trust

("Bank"). The Comptroller possesses the authority to take this action through a legislative enactment. **12 U.S.C. §203(a)**. Plaintiffs recognize that **Section 203(a)** permits the Comptroller to appoint a conservator "without notice or prior hearing" when one of eight enumerated circumstances is present.

In this case, the Comptroller based his actions on two articulated findings. First, that the Bank had violated laws and regulations and engaged in unsafe and unsound practices likely to weaken the Bank's condition and seriously prejudice the interests of the Bank's depositors. Second, that the Bank had continuously violated the terms of a November 14, 1986 Cease and Desist order. These findings authorized the Comptroller to appoint a conservator pursuant to **12 U.S.C. §203(a)(5) and 12 U.S.C. §203(a)(7)**, respectively.

Plaintiffs content that the Constitution mandate a post-seizure evidentiary hearing since they did not receive an opportunity to be heard prior to the Comptroller appointing a conservator. The plaintiffs base their argument on a number of Supreme Court cases which established that due process requires some degree of notice and an opportunity to be heard when one's property is seized by the government. See **Fuentes v. Shevin**, 407 U.S. 67, 80 (1972); **Parratt v. Taylor**, 451 U.S. 527, 539 (1981). Plaintiffs assert that some degree of due process is necessary to provide them a forum to articulate "its view of the facts."

DISCUSSION

In **Woods v. Federal Home Loan Bank Board**, 826 F.2d 1400, 1410-11 (5th Cir. 1987), a Fifth Circuit panel was faced with a substantially similar argument. In that case, dealing with the seizure of a bank's assets, the plaintiffs asserted that a post-deprivation evidentiary hearing was constitutionally mandated since the plaintiff received no notice or opportunity to respond prior to the seizure of the assets. **Id.** Additionally, in **Woods**, the plaintiffs argued that the arbitrary and capricious standard, which a court is legislatively required to apply when reviewing the actions of the Comptroller, denied them due process of law. **Id.**

In dismissing these arguments, the Fifth Circuit determined that Congress, in providing for an arbitrary and capricious standard, provided a review that is adequate to ensure against the risk of mistaken deprivation of property. **Id.** The Fifth Circuit reasoned that if the record is property compiled and demonstrates that Congressional mandates were followed, and a fair and reasoned consideration to all relevant factors occurred before a conservator was appointed, then the decision will survive district court review and that is all the process that a plaintiff is Constitutionally due. **Id.**; See. also, **Gibraltar Savings v. Ryan**, 772 F.Sup. 1290, 1292 (D.D.C. 1991).

The plaintiffs in this case continually cite the Supreme Court's decision in **Fuentes** as mandating additional process is required. 407 U.S. 67 (1972). The plaintiffs' reliance on **Fuentes** is inappropriate. In **Fuentes**, the Supreme Court was faced with a procedure whereby a

person merely had to fill in the blanks of a form in order to receive a writ of replevin, thereby seizing control of the personal property of a citizen. **Fuentes**, at 70-71. The process called for no record whatsoever, merely a blanket assertion that the property in question was being wrongfully detained. **Fuentes**, at 73-75.

In this case, prior to a conservator being appointed, the Office of the Comptroller ("OCC") generated examination reports dating back to 1988 and held meetings with the Bank, during which the OCC expressed its concerns regarding the operations of the Bank. The record also contains the Bank's responses to the examination reports generated by the OCC, which were considered by the Comptroller in deciding whether to appoint a conservator. In sum, unlike the plaintiffs in **Fuentes**, the Bank was aware of OCC's concerns and a record exists which displays that the plaintiffs were not deprived of a property interest without notice of the OCC's concerns and an opportunity to respond to those concerns.

The recent banking crisis has greatly expanded Congress' role and interest in the banking industry. Recently, Congress enacted the **Financial Institution Reform, Recovery and Enforcement Act** ("FIRREA"), which served to expand the role of the Comptroller in performing a watchdog function in the banking industry. **Pub. L. No. 101-73, §802, 103 Stat. 442 (1989).** Congressional intent in enacting FIRREA was, in part, "to strengthen the enforcement powers of Federal regulators of depository institutions." **FIRREA, § 101(9).** Part and

parcel in this desire to strengthen the enforcement power of federal regulators was the decision to broaden the Comptroller's power to appoint conservators, allowing him to take this action prior to a bank becoming insolvent.

The decision to appoint a conservator is not a judgment to divest a property owner from the property in question. **Franklin Savings Association v. Office of Thrift Supervision**, 934 F.2d 1127, 1141 (10th Cir. 1991). On the contrary, this serves as a judgment that the property owner is unable or unwilling to properly manage or control the assets, and the appointment of a conservator is an attempt to place the entity back onto solid ground. **Id.** at 1141. Appointment a conservator is within the mandate issued by Congress and comports with the Congressional intent behind the enactment of FIRREA.

This Court agrees with the analysis provided in the **Woods** decision. 826 F.2d at 1410-13. Congress provided a method to review the decision to appoint a conservator and this method is adequate to ensure against the risk of erroneous deprivation of property. **See Woods**, at 1411; **Gibraltar Savings v. Ryan**, 772 F.Supp. 1290 (D.D.C. 1991); **12 U.S.C. 203(b)(1).** The standard of review dictated by Congress allows this Court to entertain jurisdiction to determine whether the Comptroller remained within the confines of his mandate and whether the compiled administrative record displays a fair and reasoned consideration of all relevant factors occurred before a conclusion was reached that statutory grounds to appoint a conservator existed. **Woods**, at 1411.

Upon balancing Congressional intent, the risk of erroneous deprivation of property and the procedure employed in the decision to appoint a conservator, I find that this Court's Congressionally-dictated standard of review will provide all the statutory and/or Constitutional process that these plaintiffs are due.

Accordingly.

IT IS ORDERED that plaintiffs' request for a post-seizure hearing is denied.

The Clerk of Court is directed to forthwith notify the respective parties of the making of this order.

DONE and DATED this 2nd day of September, 1992.

/s/Jack D. Shanstrom
United States District Judge

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MONTANA
BILLINGS DIVISION

FIRST NATIONAL BANK & TRUST, WIBAUX, MONTANA, and ITS STOCKHOLDERS, Thomas E. Towe Trust, Karen James Trust, Kristin Hartley Trust, Sara Horsfall Trust, Andrew C. Towe Trust, Wibaux Investments, Irene Koch, and Dorothy Tow,	) Cause No. CV) 92-121-BLG-) RWA)))) Judge Jack D.) Shanstrom)
Plaintiffs,	) **MEMO-**) **RANDUM**
vs.	) **& ORDER**)
THE COMPTROLLER OF THE CURRENCY,	)))
Defendant.	)

Defendant has moved the Court for a protective order limiting review in this case to the administrative record. Plaintiffs have opposed this motion, asserting their desire to conduct discovery outside the administrative record. Upon careful consideration of the briefs and documents submitted, and having presided over oral argument, I am prepared to rule.

BACKGROUND

This case involves the validity of a decision, made by defendant Comptroller of the Currency pursuant to powers promulgated in **12 U.S.C. § 203(a)**, to appoint a conservator to take control of First National Bank and Trust ("Bank"). The Bank was ultimately seized June 25, 1992 and a record which seeks to substantiate this decision was prepared by the administrative agency. Plaintiffs filed the present litigation pursuant to **12 U.S.C. 203(b)**, seeking review of the administrative decision. The motion currently before the Court will determine the scope of discovery permitted during the course of this judicial review.

DISCUSSION

In opposing the request for a protective order, plaintiffs initially assert that discovery outside the administrative record is warranted based on the fact that a constitutional "taking" has occurred. Plaintiffs asset that cases limiting review to the administrative record under the **Administrative Procedures Act** are not applicable because a "taking" has occurred and an opportunity for a full hearing has not been afforded.

On September 2, 1992, I entered an order denying plaintiffs' motion for a post-seizure constitutional hearing in this matter. In rendering decision, I recognized the broad power that Congress provided to the Comptroller in determining the need to appoint an conservator. In the September 2, 1992 order, I found that a decision rendered by the Comptroller was reviewed employing an arbitrary and capricious standard of review.

In so holding, I determined that Congress articulated a standard of review whereby a court entertains jurisdiction to determine whether the Comptroller remained within the confines of the congressional mandate and whether the administrative record displays that a fair and reasoned examination of all relevant factors occurred before a decision to appoint a conservator was reached. Accordingly, I found that this congressionally-dictated standard of review effectively provided all the statutory and/or constitutional process to which plaintiffs are due. It is with this reasoning in mind that I find Congress has dictated a standard of review in this area and this standard limits review to the administrative record which was before the Comptroller when the decision to appoint a conservator was reached. See **Franklin Savings Association v. Director, Office of Thrift Supervision**, 934 F.2d 1127 (10th Cir. 1991), cert. den. ___ U.S. ___, 112 S.Ct. 1475 (1992); **Woods v. Federal Home Loan Bank Board**, 826 F.2d 1400 (5th Cir. 1987), cert. den. 485 U.S. 959 (1988). To find otherwise would allow this Court to substitute its judgment for that of a congressionally-empowered administrative agency.

Plaintiffs assert that if I find a review of the administrative record provides all the due process required in this case, then an exception exists to the rule that review is limited to the administrative record. The Ninth Circuit Court of Appeals recognizes four exceptions whereby discovery and review beyond the administrative record will be permitted. The first exception applies where there exists a substantial failure to explain an administrative decision, such that effective judicial review

cannot be performed. **Public Power Council v. Johnson**, 674 F.2d 791 (9th Cir. 1982). If this exception exists, the preferred approach is not to permit expanded discovery, but rather to remand the case to the agency for an expansion of the basis for the decision. **Public Power Council** at 794. In this case, such a remand is not necessary since the written decision articulated by the Comptroller substantially explains the administrative decision, allowing effective judicial review to be performed. Accordingly, the first exception allowing review outside the administrative record is inapplicable.

A second exception exists where discovery is necessary to clarify technical terms used by the agency in rendering a decision. **Public Power Council** at 794. Under this exception, additional discovery is permitted to allow the parties to define certain "technical" terms, thus allowing a better understanding of the decision rendered at the administrative level. Plaintiffs assert that the term "covered transaction", insofar as it relates to an OREO situation, needs to be clarified in order to go forth with this review. In particular, plaintiffs express a need to engage in discovery in order to ascertain why the selling of title and mortgage insurance by Towe Farms does not constitute an equivalent guarantee under **12 C.F.R. § 7.305(b).**

This argument contradicts previous assertions made by the plaintiffs. Throughout the briefs submitted, and during the time allotted for oral argument, counsel for plaintiffs repeatedly asserted that Edward Towe is a competent and experienced banker and such expertise is

responsible for the alleged turnaround of the First National Bank of Wibaux. However, in arguing the need for discovery, plaintiffs assert that certain "technical" terms need to be clarified. If Edward Towe is indeed an expert in the banking field with over fifty years of experience, it should follow that discovery to clarify a technical banking term is not necessary.

As an example of the Bank's understanding of the intricacies associated with Other Real Estate, the Comptroller's decision cites to a letter written by the Bank to a condominium purchaser. That letter stated, "Though the down payment for this unit is only $200.00, we are supposed to collect 10% down payment or $3,300 more in order to legally carry the loan on the bank's books." See **Comptroller Decision** page 47. Even more indicative of the Bank's understanding of this "technical" concept is the manner in which this 10% requirement was met. Within this same letter, the Bank stated, "What all this amounts to is Grant Investments Fund is making you a private loan of $3,300 in order that the bank's records will show that you actually paid the bank the required 10% down on the condo." These statements assist in establishing plaintiffs' understanding of this alleged "technical" term.

A second significant factor leading to the conclusion that no further discovery is necessary to explain certain "technical" terms is Towe's companies' attempt to sell insurance in order to avoid the 10% down payment requirement. Pages 48 through 56 of the Comptroller's decision are dedicated to explaining why Towe's

companies were selling insurance illegally, why this scheme is not permitted under banking regulations, and how this scheme was devised to alter reporting figures under OREO. In sum, the alleged "technical" terms, which plaintiffs point to as a basis for permitting discovery outside the administrative record, have been thoroughly addressed in the record itself. A meaningful review of this record can occur without taking the unusual step of permitting discovery in order to clarify these alleged "technical" terms.

A third exception permitting discovery outside the administrative record exists where a party asserts and demonstrates that the administrative decision was based, in part, upon documents or materials that were not made part of the administrative record. **Public Power Council** at 794. A reviewing court cannot effectively engage in a meaningful judicial review where documents considered in making the decision are not part of the administrative record. In this case, plaintiffs assert that because no formal hearing was conducted, due process principles dictate that discovery be conducted to ensure that all relevant material is brought before the reviewing court. In fashioning this argument, plaintiffs do not assert that certain documents were considered in reaching the decision without being made part of the record. Rather, plaintiffs assert that certain documents "should" have been considered by the Comptroller, but were ignored. Once again, review of the administrative record reflects that the basis for the administrative decision is clear and comprehendible. Because of this, effective judicial review evaluating whether the decision was arbitrary and

capricious can occur. In sum, plaintiffs do not assert that certain documents considered by the agency were not made part of the record. Accordingly, this exception is inapplicable.

Finally, a fourth exception permitting discovery outside the administrative record exists where there is a strong showing of bad faith on the part of the administrative agency, thus permitting discovery to explore the thought process which led to the administrative decision. I am not persuaded bad faith existed on the part of the agency. Accordingly, this exception is also inapplicable.

The final argument utilized by plaintiffs as a basis to support their contention that discovery outside the administrative record is warranted in this case is an assertion that a need for discovery exists to determine the factual basis underlying the Comptroller's decision. Plaintiffs assert a right to take the depositions of individuals who provided "unsworn statements in support of the 'decision'".

Plaintiffs recognize that top agency decision makers are exempt from the discovery process in order to protect and insure the integrity of the process. United States v. Morgan, 313 U.S. 409 (1941). However, plaintiffs assert that this same rationale does not apply to subordinates who consulted with the top level official prior to the decision being rendered.

In reviewing a decision of an administrative agency,

it is not the proper function of a court to probe the mental processes of the agency or its members. **Franklin Savings Association v. Ryan**, 922 F.2d 209, 212 (4th Cir. 1991), citing **Feller v. Board of Educ. of Conn.**, 583 F.Supp. 1526, 1528 (D.Conn. 1984). To permit discovery into the thoughts of subordinates would serve to undermine the rationale behind barring such discovery of top agency officials. Once again, I decline plaintiffs' invitation to expand the review in this matter beyond the administrative record.

The Tenth Circuit Court of Appeals has held, "the district court, in reviewing the director's decision to appoint a conservator, should confine its review to that information before the director at the time the appointment decision was made". **Franklin Savings Association v. Director, Office of Thrift Supervision**, 934 F.2d 1127, 1140 (10th Cir. 1991). Congress created a standard of review in this area to examine whether the facts relied upon by the decision maker show that a statutory ground for the appointment of a conservator existed. **Id.** at 1141. Allowing the parties to conduct discovery outside the administrative record would serve to blur this congressionally-dictated standard of review by submitting for a court's consideration facts and evidence not before agency officials when the decision to appoint a conservator was made.

In sum, I will adhere to the congressionally-dictated standard of review in this area and will review the administrative record to determine whether the decision to appoint a conservator was arbitrary and capricious.

Footnote: For further discussion of the standard of review to be applied in this case, see my order entered September 2, 1992, relating to plaintiffs' request for a "post seizure constitutional hearing".

The focus of the court in conducting such review is to examine whether sufficient evidence exists in the administrative record to form a reasoned opinion that statutory grounds for the appointment of a conservator exist. **Franklin Savings Association** at 1141. I will focus on providing such review and will not substitute my decision for that of the Comptroller.

Accordingly, **IT IS ORDERED:**

1. Defendant's motion for a protective order is granted. Review of this administrative decision shall be limited to the administrative record.]

2. Pursuant to this Court's order of September 23, 1992, counsel for plaintiffs shall have ten (10) days from the filing of this order in which to submit a brief in opposition to defendant's motion for summary judgment.

DONE and DATED this 20th day of November, 1992.

s/s Jack D. Shanstrom
United States District Judge

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MONTANA
BILLINGS DIVISION

FIRST NATIONAL BANK & TRUST, WIBAUX, MONTANA, and ITS STOCKHOLDERS, Thomas E. Towe Trust, Karen James Trust, Kristin Hartley Trust, Sara Horsfall Trust, Andrew C. Towe Trust, Grant Investments Fund, Irene Koch, and Dorothy Tow,	)	Cause No. CV 92-121-BLG-JDS
Plaintiffs,	)	
vs.	)	
THE COMPTROLLER OF CURRENCY,	)	MEMO-RANDUM & ORDER
Defendant.	)	

Counsel forthe parties appeared before the Court on March 25, 199: for oral argument on pending cross-motions for sunmary judgment. Upon consideration of the briefs submitted, the arguments advanced in open court, and a reiew of the administrative record, I find

that no genuine issues of material fact exist and am therefore prepared to rule.

ABBREVIATED FACTUAL BACKGROUND

On November 20, 1992, I issued an order on defendant's request for a protective order and addressed whether plaintiffs should be permitted to conduct discovery or whether review of the Comptroller's decision would be limited to the administrative record. In the that order, I included a lengthy section describing the factual background of this controversy. Although a brief factual background will be provided here, I refer to my order of November 20, 1992 for a more detailed description of the factual history in this litigation.

Mr. Edward Towe assumed management responsibilities of the Bank in 1987 and continued in that role until a conservator was appointed on June 25, 1992. Defendant Comptroller of the Currency (Comptroller), pursuant to his authority under 12 U.S.C. § 203(a), appointed the conservator to take possession and control of plaintiff First National Bank & Trust, Wibaux, Montana (the Bank). In a 124-page document, the Comptroller outlined the concerns underlying the appointment of a conservator. In large part, the Comptroller based the decision on a finding that: (1) the Bank violated laws and regulations, and engaged in unsafe and unsound practices likely to weaken the Banks's condition and seriously prejudice the interests of the Bank's depositors; and (2) the Bank's continuous violations of the terms of a November 14, 1986 Cease and

Desist Order. See Decision of the Comptroller of the Currency To Appoint A Conservator For the First National Bank & Trust, Wibaux, Montana (Decision).

On July 6, 1992, the Bank filed this action, pursuant to 12 U.S.C. § 203(b), challenging the decision to appoint a conservator. The Bank challenges the Comptroller's decision under 12 U.S.C. § 203(b)(1), which provides for judicial review, and provides for a setting aside of the decision to appoint a conservator "only if the court finds that such decision was arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law."

STANDARD OF REVIEW

As stated above, the Comptroller's decision to appoint a conservator is reviewed utilizing an arbitrary and capricious standard of review. See 12 U.S.C. §203(b)(1). When reviewing the Comptroller's decision, this Court must not substitute its judgment for that of the Comptroller. Citizens to Preserve Overton Park, Inc. v. Volpe, 401 U.S. 402, 416 (1971). Rather, this Court must give deference to the decision rendered by the Comptroller. Franklin Savings Association v. Director, Office of Thrift Supervision, 934 F.2d 1127, 1141 (10th Cir. 1991); cert. den., ___ U.S. ___, 112 S.Ct. 1475 (1992).

DISCUSSION

Before directly addressing contentions advanced by the parties, a brief description of the power of the Comptroller to appoint a conservator is appropriate. As

I recognized in my order issued September 2, 1992, following the recent banking crisis in this country, Congress began assuming a greater role in the banking industry. Part of this increased role is reflected in the enactment of the **Financial Institution Reform, Recovery, and Enforcement Act, ("FIRREA")**, which expands the role of the Comptroller in policing the banking industry. This legislative enactment vested the Comptroller with the ability to appoint a conservator prior to a bank becoming insolvent. The obvious intent in expanding the powers of the Comptroller was to provide further safeguards for the banking public.

The decision to appoint a conservator serves as a judgment that the current operator is unable to properly manage the bank's assets, and the decision to appoint a conservator serves to protect the bank's depositors by placing the entity back onto solid ground. **Franklin Savings Association v. Office of Thrift Supervision**, 934 F.2d 1127, 1141 (10th Cir. 1991). In this case, the decision to appoint a conservator was made, and the plaintiffs, through this action, challenge the Comptroller's decision.

Regardless of plaintiffs' assertions to the contrary, it is not the Court's role to closely scrutinize the decision-making ability of the Comptroller given this particular set of facts. Rather, the Court's role is to determine whether the Comptroller, when making the decision to appoint a conservator, remained within his Congressionally-dictated mandate, and whether the administrative record reflects that a fair and reasoned consideration of all relevant

factors occurred before the Comptroller made the decision to appoint a conservator. See **Woods v. Federal Home Loan Bank Board**, 826 F.2d 1400, 1411 (5th Cir. 1987).

1. **Review of the Comptroller's determination that the Bank violated 12 U.S.C. § 371(c).**

Plaintiffs initially attack the Comptroller's determination that the Bank was engaged in unsafe and illegal practices which were likely to weaken the Bank's condition or otherwise seriously prejudice the interests of its depositors.

First, plaintiffs argue that the administrative record does not support the Comptroller's finding that the Bank violated **12 U.S.C. § 371(c)**. This Code section prohibits a national bank from engaging in transactions with affiliates on terms that are more favorable than those prevailing for non-affiliated parties. Id. The administrative record reflects the Comptroller's finding that Grant Investments, an entity controlled by Edward Towe, was an affiliate of the Bank and that the relationship between Grant Investments and the Bank is riddled with favorable treatment, in violation of **12 U.S.C. § 371(c)**. See Decision of the Comptroller of the Currency, at page 14.

Specifically, the Comptroller alluded to a finding that Grant Investments is a "financial institution within a financial institution." Decision of the Comptroller of the Currency, at page 12. The Comptroller found that the Bank permitted Grant Investments to maintain its offices at the Bank rent free, use Bank stationery, conduct business using Bank employees and computer equipment,

and that Grant Investments provided free checking accounts, through the Bank, to each of the partners of Grant Investments. Id. at 12-13. These checking accounts were provided without service charges, overdraft charges, or charges of any kind. Id. at 13. After conducting a review of the relationship between these two entities, the Comptroller concluded that entanglement was so great that it becomes difficult to determine which assets belonged to the Bank and which assets belonged to Grant Investments. Id. at 15. Plaintiffs argue that there was no violation of **12 U.S.C. § 371(c)** since Grant Investments was not an "affiliate" of the Bank for purposes of this code section. Plaintiffs spend considerable time discussing the technicalities associated with the definition of "affiliate," and attempt to portray Grant Investments as not falling under this definition. Despite plaintiffs' assertions to the contrary, when applying an arbitrary and capricious standard of review, I do not find error in the Comptroller's conclusions. Furthermore, I agree with the Comptroller's conclusion that, "[e]ven if not in violation of **12 U.S.C. § 371(c)**, the relationship between Grant Investments and the Bank is an unsafe or unsound condition which has severe implications of the Bank and its depositors." Decision of the Comptroller of the Currency, at page 15. I find no error in the administrative record as to the Comptroller's conclusions regarding the unusual relationship between Grant Investments and the Bank.

2. Review of the Comptroller's conclusion that there were violations of 12 C.F.R. § 7.3025.

Next, plaintiffs attack the Comptroller's finding that the Bank violated **12 C.F.R. § 7.3025(b)**. This regulation mandates that when a bank acquires property (i.e. through

default or foreclosure), that bank must dispose of these properties within five years. If a bank sells this acquired property, it cannot be entered on the books as a valid bank loan unless it receives 10% down payment or a guarantee of the 10% down payment. Until this 10% of the total sales price requirement is met, the loan is considered a "covered transaction," and it must be included in the other real estate owned (OREO) section of Call reports. Classification of property as OREO property is essential for accounting purposes and, in particular, to ensure that the property is regularly and properly appraised.

In this case, the Comptroller determined that the Bank engaged in two "schemes" to circumvent rules and regulations concerning OREO. Decision of the Comptroller of the Currency, at page 32. The first alleged scheme involved using Grant Investments to finance down payments on OREO condominiums. The second alleged scheme involved using another entity, Towe Farms, to issue mortgage insurance to OREO condominiums so as to meet the 10% guarantee requirement and, therefore, allow the Bank to remove the OREO condominiums from the covered transaction category.

Plaintiffs admit that the Bank permitted Grant Investments to loan each of the OREO condominium purchasers enough capital to make a 10% down payment. Plaintiffs argue that once this 10% down payment was in the Bank's possession, the sale of these units was not a covered transaction. The Comptroller disagreed with plaintiffs' argument and, as a result, required the Bank to pay off each of the Grant Investments loans. I find no error in the Comptroller's interpretation of the applicable regulation in this situation.

Plaintiffs next assert yet another "exception" within the regulation by attempting to satisfy the 10% down payment through the use of a guarantee. Another entity, Towe Farms, was used to issue mortgage insurance to the condominium purchasers guaranteeing payment of the required 10% down payment. It is undisputed that Towe Farms does not have a license or other state authorization to issue such insurance. It is also undisputed that without guarantee contracts, the Bank is in violation of § 7.3025(b).

Plaintiffs argue that although Towe Farms may be at fault for issuing insurance without a license, the issued insurance contracts are enforceable and are not null and void. Therefore, plaintiffs argue, the Bank is fully protected against loss by the insurance contracts issued by Towe Farms since the Bank has the ability to enforce these contracts.

Defendant asserts that a contract in violation of law is null and void, see Shlay v. Montgomery, 802 F.2d 918, 922 (7th Cir. 1986), and that the insurance issued by Towe Farms cannot qualify as the equivalent of insurance legally issued by a licensed insurer. After reviewing the arguments advanced by the parties on this issue, I find no basis upon which to dispute the Comptroller's conclusions.

The Comptroller concluded that the arrangement whereby Towe Farms provided insurance guarantees for purposes of 12 C.F.R. § 7.3025(b). "At times, no insurance proceeds were paid to the Bank, and, when they were, the Bank often reimbursed Towe Farms." Decision of the Comptroller of the Currency, at page 55. The Comptroller concluded that, in effect, "Towe Farms was 'insuring' the Bank against loss, but the Bank was

indemnifying Towe Farms for the insurance proceeds paid." Id.

After a review of the record, I agree with the Comptroller that the arrangement whereby Towe Farms provided insurance contracts for the sale of these condominiums was part of a scheme employed to remove this property from the covered transaction status. See Id. at 55-56. Applying an arbitrary and capricious standard of review, I find no error in the Comptroller's determination that the Towe Farms guarantees were not equivalent to private mortgage insurance, in accordance with 12 C.F.R. § 7.302(b).

3. Review of the Comptroller's determination that the Bank engaged in other unsafe and illegal practices which were likely to weaken the Bank's condition and seriously prejudice the interests of its depositors.

As a final line of attack, plaintiffs dispute the Comptroller's determination that the Bank engaged in other transactions which were either unsafe or illegal, and which were likely to weaken the Bank's condition and seriously prejudice the interests of its depositors. Among the transactions listed by the Comptroller as additional basis to support the decision to appoint a conservator are those labeled the "New Year's Day transaction" and the "Jacobsen transaction."

The New Year's Day transaction "involved the payment of two checks, each in an amount equal to more than one half the Bank's capital, against uncollected funds, utilizing federally insured deposits." Decision of the Comptroller of the Currency, at page 15. Essentially, this transaction came about after the IRS informed Towe

Foundation that it would incur penalties if it remained a partner in Grant Investments. Id. at page 16. To avoid these penalties, Towe Foundation needed to liquidate its interest in Grant Investments.

To accomplish this, Grant Investments tendered a check, made out to Towe Foundation, in the amount of $994,500.00. Although Grant Investments had approximately $11,000.00 in its accounts at the time, the check made out to Towe Foundation was paid by the Bank and deposited into Towe Foundation's account at the Bank. On the same day, Towe Foundation wrote a check to Grant Investments in the amount of $994,561.00. Once again, although Towe Foundation had approximately $3,000.00 in its account at the time, this check was paid, and the funds were deposited in Grant Investments' account at the Bank.

Plaintiffs respond to the allegations concerning the New Year's Day transaction by asserting that there was no exposure to the Bank as a result of this highly unusual transaction. Despite plaintiffs' assertions to the contrary, I agree with the Comptroller's conclusion that while it is fortunate that no funds were lost as a result of this transaction, this type of transaction poses significant risks to both the Bank and its depositors. See Decision of the Comptroller of the Currency, at page 17. Accordingly, applying an arbitrary and capricious standard to the Comptroller's conclusions regarding the New Year's Day transaction, I do not find the existence of error.

I reach a similar conclusion regarding the Jacobsen transaction. Briefly, the Jacobsen transaction involved the "sale" of real estate between Grant Investments and Jacobsen. See Decision of the Comptroller, at page 20-

21. The Bank was a conduit for this transaction, whereby the Bank loaned Jacobsen funds and Grant Investments, in turn, purchased this loan. Although this transaction could have been conducted without the Bank, Edward Towe (Bank President and Grant Investments manager) stated that, "the Bank was involved in this transaction because he made it involved." Id. at 21. Edward Towe further acknowledged, "he (Towe) doesn't know of any benefit to the Bank from being involved in the transaction, and he (Towe) acknowledged that the Bank did not make a profit from this transaction." Id.

Plaintiffs again assert that no loss to the Bank resulted from the Jacobsen transaction. However, I am unpersuaded by this "no harm, no foul" argument and agree with the conclusion of the Comptroller, who stated:

> The Jacobsen transaction, like the New Year's Day transaction, is the result of Bank accommodations of Grant Investments. This unsafe or unsound practice prejudices the interests of depositors as Bank assets, comprised primarily of depositors' money, are being put at risk to run these sham transactions for Grant Investments through the Bank.

Id. at 23.

4. Review of the Comptroller's determination that the Bank willfully and continually violated a previously issued cease and desist order.

On November 14, 1986, the Bank consented to the issuance of a cease and desist order. The Comptroller based the decision to appoint a conservator, in part, upon a "five-year pattern of continuing violations of the 1986

Cease and Desist order . . ." Decision of the Comptroller of the Currency, at page 111. While plaintiffs dispute that such violations occurred, after a review of the record in this case, I find no error in the Comptroller's conclusions. Furthermore, plaintiffs' argument that the purpose of the Cease and Desist order has been accomplished thereby rendering any alleged violations irrelevant is not persuasive.

CONCLUSION

Simply put, when applying an arbitrary and capricious standard of review, I find no basis upon which to support a determination that the Comptroller's conclusions were not warranted in this case. After reviewing the record, I find that the Comptroller, when making the decision to appoint a conservator, remained within the Congressionally-dictated mandate. I further find that the administrative record reflects that a fair and reasoned consideration of all relevant factors occurred before the Comptroller made the decision to appoint a conservator. Therefore, the June 24, 1992 decision by the Comptroller of the Currency will remain intact.

In accordance with the above,

IT IS ORDERED:

1. Plaintiffs' motion for summary judgment is denied.

2. Defendant's motion for summary judgment is granted and the Clerk of Court is hereby directed to enter summary judgment in favor of the defendant.

The Clerk of Court is further directed to forthwith notify the respective parties of the making of this order.

DONE and DATED THIS 9th day of August, 1993.

\s\ Jack D. Shanstrom
United States District Judge

FILED, ENTERED AND NOTED
IN CIVIL DOCKET

LOU ALEKSICH, JR., CLERK

By _____
Deputy

UNITED STATES DISTRICT COURT

DISTRICT OF MONTANA BILLINGS DIVISION

JUDGMENT IN A CIVIL CASE

FIRST NATIONAL BANK & TRUST, WIBAUX, MT & its STOCKHOLDERS - Plaintiffs

V.

COMPTROLLER OF THE CURRENCY, Deft.

CASE NUMBER: CV 92-121-BLG-JDS

☐ **Jury Verdict.** This action came before the Court for a trial by jury. The issues have been tried and the jury has rendered its verdict.

☒ **Decision by Court.** This action came to trial or hearing before the Court. The issues have been tried or heard and a decision has been rendered.

IT IS ORDERED AND ADJUDGED
Plaintiffs' Motion for Summary Jmt is denied and Deft.'s Motion for Summary Judgment is granted.

(COURT SEAL)

August 9, 1993
Date

LOU ALLKSICH, JR.
Clerk

/s/ Rayna M. Weiss
(By) Deputy Clerk

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MONTANA
BILLINGS DIVISION

FIRST NATIONAL BANK & TRUST, WIBAUX, MONTANA, and ITS STOCKHOLDERS, Thomas E. Towe Trust, Karen James Trust, Kristin Hartley Trust, Sara Horsfall Trust, Andrew C. Towe Trust, Grant Investments Fund, Irene Koch, and Dorothy Tow,	)	Cause No. CV 92-121-BLG-JDS
Plaintiffs,	)	
vs.	)	
THE COMPTROLLER OF CURRENCY,	)	**MEMO-RANDUM & ORDER**
Defendant.	)	

Pending before the Court is plaintiffs' motion to alter or amend the judgment entered in this matter on August 9, 1993. Having considered the arguments and briefs of the parties, I find plaintiffs' motion should be denied.

The thrust of plaintiffs' motion is that the Court misunderstood facts underlying the Comptroller's determination that the Bank engaged in unsafe and illegal practices, and that the Court erred in not determining that the Comptroller's decision was arbitrary and capricious. I do not find plaintiffs' arguments persuasive.

Plaintiffs also assert that this Court erred in not determining that the Comptroller's seizure of plaintiffs' property without prior notice and hearing violated plaintiffs' constitutional rights. In support of their position, plaintiffs cite the recent United States Supreme Court decision in **United States v. James Daniel Good Real Property**, 62 U.S.L.W. 4013 (1993). I do not agree that the **James Daniel Good Real Property** decision indicates that the Comptroller's specific statutory authority to appoint conservators without notice or prior hearing pursuant to **12 U.S.C. § 203(a)** is a constitutional violation.

Accordingly,

IT IS ORDERED that plaintiffs' motion to amend or alter the judgment of this Court is denied.

The Clerk of Court shall forthwith notify the parties of the making of this order.

DONE AND DATED this 25th day of February, 1994.

Jack D. Shanstrom
United States District Judge

FIRST NATIONAL BANK & TRUST, WIBAUX, MONTANA; Thomas E. Towe, Trust; Kristin Hartley, Trust; Sara Horsfall, Trust; Andrew C. Towe, Trust; Grant Investments Fund; Irene Koch; Dorothy Tow, Stockholders of First National
Bank of Wibaux, Montana,

Plaintiffs-Appellants,

v.

DEPARTMENT OF the TREASURY, The COMPTROLLER OF THE CURRENCY,

Defendant-Appellee.

No. 94-35283.

United States Court of Appeals, Ninth Circuit.

Argued and Submitted May 3, 1995.

Decided Aug. 21, 1995.

Bank and certain of its shareholders sued comptroller of the currency to terminate conservatorship over bank. The United States District Court for the District of Montana, Jack D. Shanstrom, J., granted summary judgment for comptroller, and bank appealed. The Court of Appeals, David R. Thompson, Circuit Judge, held that: (1) lack of predeprivation notice and hearing did not violate due process; (2) district court's postdeprivation

review was limited to administrative record; (3) district court's postdeprivation review did not violate due process; and (4) comptroller did not act arbitrarily or capriciously in placing bank in conservatorship.

Affirmed.

*894 Thomas E. Towe, Towe, Ball, Enright, Mackey & Sommerfield, Billings, MT, for plaintiffs-appellants.

*895 Jacob M. Lewis, U.S. Dept. of Justice, Washington, DC, for defendant- appellee.

Appeal from the United States District Court for the District of Montana.

Before: WRIGHT, SKOPIL and THOMPSON, Circuit Judges.

DAVID R. THOMPSON, Circuit Judge:

Acting Comptroller of the Currency Stephen L. Steinbrink (the Comptroller) appointed a conservator for First National Bank & Trust (the Bank) pursuant to 12 U.S.C. s 203(a) (Supp. II 1990). The Bank and certain of its shareholders sued the Comptroller to terminate the conservatorship, contending he had violated their rights to procedural due process and had acted arbitrarily and capriciously. On cross-motions for summary judgment, the district court granted judgment for the Comptroller, from which the Bank appeals. We affirm.

FACTS

On January 15, 1987, Edward Towe became president and chief executive officer of First National Bank and Trust, located in eastern Montana. [FN1] At that time, the Bank was operating under a November 14, 1986 cease and desist order imposed by the Comptroller.[1]

Between 1987 and 1990, the Comptroller issued increasingly critical examination reports of the Bank, pointing out the Bank's noncompliance with certain laws and regulations and with the terms of the cease and desist order.

In a May 5, 1992 letter to the Bank's board of directors, the Comptroller described the Bank's "history of complying with banking laws and regulations, compliance with the Cease and Desist Order and operations of the bank" as "unacceptable," and informed the board that the most recent examination revealed that the Bank's condition "remains a serious supervisory concern." The letter stated that "[d]ue to the seriousness of the matters discussed" in the letter and the accompanying examination report, the board should respond "no later than May 26, 1992."

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[1]The Towe family's control of the Bank was not limited to Edward Towe's top management position. At the time the conservator was appointed, the entire acting board of directors consisted of Towe family members, and the Towe family controlled more than 98% of the Bank's stock.

The board's response consisted of a six-page letter dated May 15, 1992 from Edward Towe as the Bank's president, a four-page letter dated June 1, 1992 from Thomas Towe, as the Bank's attorney and chairman of the board, and a 33-page "Board Response," which was enclosed with Thomas Towe's letter. On June 25, 1992, the Comptroller appointed a conservator for the Bank pursuant to 12 U.S.C. s 203(a) (Supp. II 1990).[2]

In his 124-page decision appointing a conservator, the Comptroller criticized the Bank for granting favorable treatment to its affiliated entity, Grant Investments. Also singled out for criticism was the Bank's alleged disregard of regulations governing "other real estate owned" (OREO). The Comptroller found the Bank had exceeded the five-year holding deadline for certain foreclosed properties, and that by refusing to account for those properties in accordance with banking regulations, the Bank had effectively overstated its capital. The Comptroller also found the Bank had violated at least eight of the seventeen articles of the cease and desist order.[3]

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[2]In 1991, 12 U.S.C. ss 203(a)(5) and (a)(7) were recodified at 12 U.S.C. ss 1821(c)(5)(H) and (c)(5)(D) (1994), respectively. See Federal Deposit Insurance Corporation Improvement Act of 1991 (FDICIA), Pub.L. No. 102-242, s 133(c), 105 Stat. 2271. Because these amended provisions did not become effective until December 19, 1992, and the Comptroller took over the Bank on June 25, 1992, they do not apply to this case.

[3]Other grounds for the decision included the Bank's retention of Edward Towe's wife as a "consultant," sham transactions between the

On July 6, 1992, the Bank and certain of its shareholders sued the Comptroller in district court to terminate the conservatorship pursuant to 12 U.S.C. s 203(b)(1). The Bank also requested a post-seizure evidentiary hearing, which the district court denied. The *896 Comptroller then moved for a protective order limiting review of his decision to the administrative record, which the district court granted over the Bank's opposition.

The parties filed cross-motions for summary judgment. The district court granted summary judgment to the Comptroller. The Bank moved for reconsideration, which the district court denied. This appeal followed.

DISCUSSION

A. Did the lack of predeprivation notice and a hearing violate due process?

The Comptroller is authorized to appoint a conservator for a national bank "without notice or prior hearing" whenever he finds "a violation or violation of laws, rules, or regulations, or any unsafe or unsound practice ... likely to cause insolvency or substantial dissipation of assets or earnings, or ... likely to weaken the bank's condition or otherwise seriously prejudice the interests of its depositors." 12 U.S.C. s 203(a)(5) (Supp. II 1990).

Bank and Edward Towe's associates, and the Bank's irregular compensation of Edward Towe.

The Bank contends that unless section 203(a) is limited to "extraordinary" circumstances, the Comptroller's appointment of a conservator without notice and a prior hearing is unconstitutional. See United States v. James Daniel Good Real Property, 510 U.S. ----, ----, 114 S.Ct. 492, 501, 126 L.Ed.2d 490 (1993) ("We tolerate some exceptions to the general rule requiring predeprivation notice and hearing, but only in extraordinary situations where some valid governmental interest is at stake that justifies postponing the hearing until after the event.") (quoting Fuentes v. Shevin, 407 U.S. 67, 82, 92 S.Ct. 1983, 1995, 32 L.Ed.2d 556 (1972)). Because the Bank was not afforded notice and a hearing prior to the Comptroller's appointment of the conservator, the Bank argues section 203(a) was unconstitutionally applied to it.

[1] A predeprivation hearing may be postponed "where some valid governmental interest is at stake." Good, 510 U.S. at ----, 114 S.Ct. at 501 (quoting Fuentes, 407 U.S. at 82, 92 S.Ct. at 1995). Whether a situation warrants such a postponement depends on balancing three factors: (1) the importance of the private interest affected by the governmental action, (2) the government's interests, and (3) the risk of erroneous deprivation. Id. (citing Mathews v. Eldridge, 424 U.S. 319, 335, 96 S.Ct. 893, 903, 47 L.Ed.2d 18 (1976)).

[2] It is well-recognized that the government's interest in protecting bank depositors and the public weal justifies the appointment of a conservator without a prior hearing. See Fahey v. Mallonee, 332 U.S. 245, 253-54, 67 S.Ct. 1552, 1555-56, 91 L.Ed. 2030 (1947); Fidelity Sav. &

Loan Ass'n v. Federal Home Loan Bank Bd., 689 F.2d 803, 811 (9th Cir.1982); cert. denied, 461 U.S. 914, 103 S.Ct. 1893, 77 L.Ed.2d 283 (1983). The Bank nonetheless dismisses the government's interest here as weak, because the Bank "was not on the verge of collapse." Yet the Bank was obviously troubled; its CAMEL rating, though recently upgraded, was but one grade above the worst. [FN4] Moreover, less drastic enforcement measures, including the cease and desist order, had been unavailing. Against this background, the government had a strong interest in moving quickly to avoid dissipation of the Bank's assets.[4]

Nor is the private interest in this case as strong as the Bank suggests. The Bank's shareholders had full knowledge "of the extensive regulatory system and the possibility of continuous, in-depth supervision by Bank Board examiners;" the Bank was operating under a cease and desist order and had a poor record of compliance with banking laws and regulations. See Woods v. Federal Home Loan Bank Bd., 826 F.2d 1400, 1411 (5th Cir.1987), cert. denied, 485 U.S. 959, 108 S.Ct. 1221, 99 L.Ed.2d 422 (1988). Finally, as we discuss infra, the availability and

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[4]CAMEL is a uniform rating system which reflects the condition of a financial institution. Shortly before the conservatorship, the Bank's CAMEL rating was upgraded from 5 to 4. A CAMEL rating of 4 applies to banks with "an immoderate volume of serious financial weaknesses or a combination of other conditions that are unsatisfactory," and that may have "[m]ajor and serious problems or unsafe and unsound conditions ... which are not being satisfactorily addressed or resolved." 5 Fed. Banking Law Rep. (CCH) P 59,205B, at 37,107-5 (Oct. 28, 1994).

nature of postdeprivation review by the district *897 court minimized the risk of an erroneous deprivation.

Having weighed the relevant factors, we conclude the Bank's constitutional rights were not violated by the Comptroller's appointment of a conservator without notice and a predeprivation hearing. We next consider the adequacy of the district court's postdeprivation review.

B. Was the scope of the district court's postdeprivation review consistent with section 203 and the Administrative Procedures Act?[5]

[3] Generally, judicial review of an agency decision is limited to the administrative record. Camp v. Pitts, 411 U.S. 138, 142, 93 S.Ct. 1241, 1244, 36 L.Ed.2d 106 (1973) (per curiam). However, the Bank contends section 203 required the district court in this case to depart from this general rule, expand the scope of its review beyond the administrative record, and hold an evidentiary hearing.

[4] Judicial review of the Comptroller's decision to appoint a conservator is afforded by section 203(b)(1). This section permits a bank to file suit in federal district court to terminate the conservatorship, and authorizes

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[5]"The scope of judicial review refers merely to the evidence the reviewing court will examine in reviewing an agency decision." Franklin Savings Ass'n v. Director, Office of Thrift Supervision, 934 F.2d 1127, 1136 (10th Cir.1991), cert. denied, 503 U.S. 937, 112 S.Ct. 1475, 117 L.Ed.2d 619 (1992). By contrast, "[t]he standard of judicial review refers to how the reviewing court will examine that evidence." Id.

"the court, upon the merits [to] dismiss such action or [to] direct the Comptroller to terminate" the conservatorship if it should "find[ ] that such decision was arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law." 12 U.S.C. s 203(b)(1).

Arguing for an expanded scope of review, the Bank relies on several district court cases which have read the phrase "upon the merits" in section 203(b)(1) and in 12 U.S.C. s 1464(d)(6)(A) (1988) (current version at 12 U.S.C. s 1464(d)(2)(B) (1994)), an identically-worded statute applicable to thrifts, as requiring such a hearing. See Collie v. Federal Home Loan Bank Bd., 642 F.Supp. 1147, 1149-52 (N.D.Ill.1986); Telegraph Savings and Loan Assoc. v. FSLIC, 564 F.Supp. 862, 868-70 (N.D.Ill.1981); [FN6] see also Haralson v. Federal Home Loan Bank Bd., 655 F.Supp. 1550, 1559-60 (D.D.C.1987) (12 U.S.C. s 1464(d)(6)(A) requires postdeprivation hearing in which board carries evidentiary burden), appeal dismissed, 837 F.2d 1123 (D.C.Cir.1988); Fidelity Savings and Loan Assoc. v. Federal Home Loan Bank Bd., 540 F.Supp. 1374, 1377 (N.D.Cal.1982) ("If it means nothing more, the term 'on the merits' reveals that a proceeding under this statute is more in the nature of a de novo review than an appellate review."), rev'd on other grounds, 689 F.2d 803 (9th Cir.1982), cert. denied, 461 U.S. 914, 103 S.Ct. 1893, 77 L.Ed.2d 283 (1983).[6]

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[6]These courts did not reach a consensus, however, on the exact scope of review to be afforded. Compare, e.g., Telegraph Savings, 564 F.Supp. at 869-70 (requiring full trial "on the merits") with Collie, 642 F.Supp. at 1149-52 (rejecting limiting its review to the administrative

The Fifth, Eighth and Tenth Circuits have rejected these district court cases, and have held that the phrase "upon the merits" does not require departing from the traditional scope of review. [FN7] Franklin Savings Ass'n v. Director, Office of Thrift Supervision, 934 F.2d 1127, 1140 (10th Cir.1991), cert. denied, 503 U.S. 937, 112 S.Ct. 1475, 117 L.Ed.2d 619 (1992); Woods, 826 F.2d at 1409; Guaranty Sav. & Loan v. Federal Home Loan Bank Bd., 794 F.2d 1339, 1342 (8th Cir.1986). These circuits have construed the phrase "upon the merits" as requiring neither "a full adversarial and evidentiary hearing, nor ... de novo review of appointment decisions." Franklin, 934 F.2d at 1138. As the Franklin court explained, "[r]eview 'upon the merits' ***898** simply means the district court's decision to either dismiss the action or remove the conservator should be based upon the merits of the action (i.e., whether statutory grounds for the appointment of a conservator exist), rather than on procedural or policy oriented grounds." Id. (citing Guaranty Sav. & Loan, 794 F.2d at 1342).[7]

[5] We agree with these circuit court decisions. Section 203(b)(1) does not require a district court to

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record, but holding nonetheless that if the thrift had a "meaningful opportunity to be heard" and a reasonable basis existed for the takeover, no trial was required).

[7]The Sixth Circuit, in a recent unpublished decision, followed its sister circuits in holding that the scope of review under 12 U.S.C. s 1464(d)(2)(C)(iii) is confined to the administrative record. See Marietta Franklin Securities Co. v. Muldoon, 1994 WL 399550, * 2 (6th Cir. Aug. 1, 1994) (per curiam).

expand the scope of review beyond the administrative record. The Bank argues, however, that an expanded scope of review was required in this case because when the Comptroller appointed the conservator he acted in bad faith. The Bank contends the Comptroller compiled a one-sided record by considering only agency documents and by secretly excluding relevant evidence favoring the Bank. We reject this argument.

The record reveals that the Comptroller considered the "substance" of the Bank's position before appointing a conservator. See Franklin, 934 F.2d at 1139-40 (rejecting argument that agency record was "one-sided and fail[ed] to contain any of [the thrift's own] documents," because the "substance of [the thrift's] positions were [sic] before the [agency] when the appointment decision was made"); see also Woods, 826 F.2d at 1412-13 (rejecting thrift's claims that, inter alia, agency's investigation was "wholly inadequate," and the record was "unilaterally and secretly compiled" because thrift had opportunity to rebut agency's criticism during its examinations and in connection with cease and desist proceedings).

The Bank had ample opportunity to express its views when it received adverse examinations between 1986 and 1992, and when it responded to the Comptroller's May 5, 1992 letter and accompanying examination findings. The agency record "contains numerous recitations of [the Bank's] views and reasons therefor." Franklin, 934 F.2d at 1139; see also Woods, 826 F.2d at 1412-13.

Moreover, the Bank has failed to identify any

extraordinary circumstances sufficient to override the discretion accorded the Comptroller's compilation of the administrative record. What the Tenth Circuit said in Franklin applies to this case: Absent extraordinary circumstances, the decision of the [Comptroller] as to what information he must review to make an appointment decision should be left to his discretion. The [Comptroller], in the case of judicial review of his appointment decision, has the obligation to produce and certify the record upon which he relied at the time of the decision. This record must contain sufficient data to allow the reviewing court to determine whether the [Comptroller] had a rational basis for the appointment decision. Franklin, 934 F.2d at 1139. Here, the Comptroller had a rational basis for his decision. The evidence the Bank cites as "missing" from the administrative record would not have changed that decision.

We also reject the Bank's argument that under the Administrative Procedures Act (APA), the district court should have allowed the Bank to supplement the administrative record. None of the APA-recognized exceptions to the general rule limiting judicial review to the administrative record apply in this case. See Animal Defense Council v. Hodel, 840 F.2d 1432, 1436-37 (9th Cir.1988), as amended, 867 F.2d 1244 (9th Cir.1989).

In sum, neither section 203, the Bank's claim of bad faith, nor the APA, required the district court to review the Comptroller's decision on the basis of anything other than the administrative record. We turn now to the

Bank's argument that the district court's postdeprivation review of the administrative record violated due process.

C. Did the district court's postdeprivation review violate due process?

[6] The Bank grounds its due process challenge on its assertion that the postdeprivation review was constitutionally inadequate because, by refusing to consider evidence outside of the administrative record, the district court failed to "assure against the risk of a mistaken deprivation." We reject the Bank's due process challenge.

At every turn the Bank had the opportunity to respond to the Comptroller's concerns. The Bank received the Comptroller's unfavorable ***899** examination reports, it had discussions with Comptroller personnel, and prior to the conservator's appointment, it was given the opportunity to respond to the Comptroller's findings. See Woods, 826 F.2d at 1411-13; see also Memphis Light, Gas & Water Div. v. Craft, 436 U.S. 1, 16 n. 17, 98 S.Ct. 1554, 1564 n. 17, 56 L.Ed.2d 30 (1978) ("The opportunity for informal consultation with designated personnel empowered to correct a mistaken determination constitutes a 'due process hearing' in appropriate circumstances."). The Bank "understood the issue" and had "full opportunity to justify [its] conduct." Southwest Sunsites, Inc. v. F.T.C., 785 F.2d 1431, 1435 (9th Cir.) (internal quotation omitted), cert. denied, 479 U.S. 828, 107 S.Ct. 109, 93 L.Ed.2d 58 (1986). The Bank's responses were made part of the administrative record,

and were considered by the Comptroller before he appointed the conservator.

The Bank's due process rights were further safeguarded at the district court hearing. There the Bank had ample opportunity to argue its position and to rebut the Comptroller's conclusions before an impartial tribunal. That no new evidence was introduced is inconsequential. Cf. Clouser v. Espy, 42 F.3d 1522, 1540-41 (9th Cir.1994) (holding that evidentiary hearings are not required by due process when administrative agency includes written submissions in administrative record and provides for appellate administrative review), cert. denied, --- U.S. ----, 115 S.Ct. 2577, 132 L.Ed.2d 827 (1995). The Bank's due process rights were not violated.

D. Did the Comptroller act arbitrarily and capriciously by placing the Bank in conservatorship?

[7] The willful or continuing violation of a cease and desist order independently warrants appointment of a conservator, regardless of whether such violations place a bank at financial risk. 12 U.S.C. s 203(a)(7). Focusing on the Comptroller's findings, the Bank argues the Comptroller erred in finding that it violated numerous provisions of the cease and desist order. As a result of these erroneous findings, the Bank contends the Comptroller acted arbitrarily and capriciously when it placed the Bank in conservatorship.

Under our "narrow" standard of review, Marsh v. Oregon Natural Resources Council, 490 U.S. 360, 378, 109

S.Ct. 1851, 1861-62, 104 L.Ed.2d 377 (1989), we may not "substitute [our] judgment for that of the agency," Motor Vehicle Manuf. Ass'n v. State Farm Mut. Auto. Ins. Co., 463 U.S. 29, 43, 103 S.Ct. 2856, 2867, 77 L.Ed.2d 443 (1983), but instead must determine whether the agency "has considered the relevant factors and articulated a rational connection between the facts found and the choice made." Baltimore Gas & Elec. Co. v. Natural Resources Defense Council, Inc., 462 U.S. 87, 105, 103 S.Ct. 2246, 2256, 76 L.Ed.2d 437 (1983).

The Bank admits violating various policies which it had adopted pursuant to the cease and desist order, yet insists it did not violate the cease and desist order. The Bank contends the order required only "adoption," not actual implementation, of the policies. Therefore, the Bank reasons, its failure to abide by those policies amounted to just that, a violation of the policies, not the terms of the cease and desist order.

This argument is without merit. As the Comptroller puts it, "the Bank's reading would render the cease and desist order meaningless; there is no point in having the Bank adopt a comprehensive revision of its policies and practices if the Bank is not obliged to abide by" them.

The Bank's violations of the cease and desist order alone justified the appointment of a conservator. The Comptroller's appointment of a conservator was not

arbitrary or capricious.[8]

CONCLUSION

The Comptroller's ex parte appointment of a conservator without notice and a predeprivation ***900** hearing did not violate due process. Limiting judicial review to the administrative record did not violate due process, 12 U.S.C. s 203, or the APA. The Bank's violations of the Comptroller's cease and desist order warranted the appointment of a conservator. That appointment was not arbitrary or capricious.

AFFIRMED.

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[8]Because the Bank violated the cease and desist order, we need not determine whether the conservatorship was also justified by the Bank violating banking laws and regulations. See Franklin, 934 F.2d at 1142 (observing that appointment of conservator withstands judicial review when one of the statutory grounds existed at the time of the appointment).

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

FIRST NATIONAL BANK & TRUST, Wibaux, Montana; THOMAS E. TOWE Trust; KRISTIN HARTLEY Trust; SARA HORSFALL Trust; ANDREW C. TOWE Trust; GRANT INVESTMENTS FUND; IRENE KOCH; TOW, Stockholders of First National Bank of Wibaux, Montana,	)	No. 94-35283 D.C. No. CV-92-00121-JDS **ORDER**
Plaintiffs-Appellants,	)	
vs.	)	
DEPARTMENT OF THE TREASURY, The Comptroller of the **Currency,**	)	
Defendant-Appellee.	)	

FILED
OCT 30, 1995

LOU ALEKSICH, JR., Clerk

By .....
Deputy Clerk
Before: WRIGHT, SKOPIL and THOMPSON, Circuit Judges.

The panel, as constituted above, has unanimously voted to deny the petition for rehearing. Judge Thompson voted to reject the suggestion for rehearing en banc, and Judges Wright and Skopil so recommend.

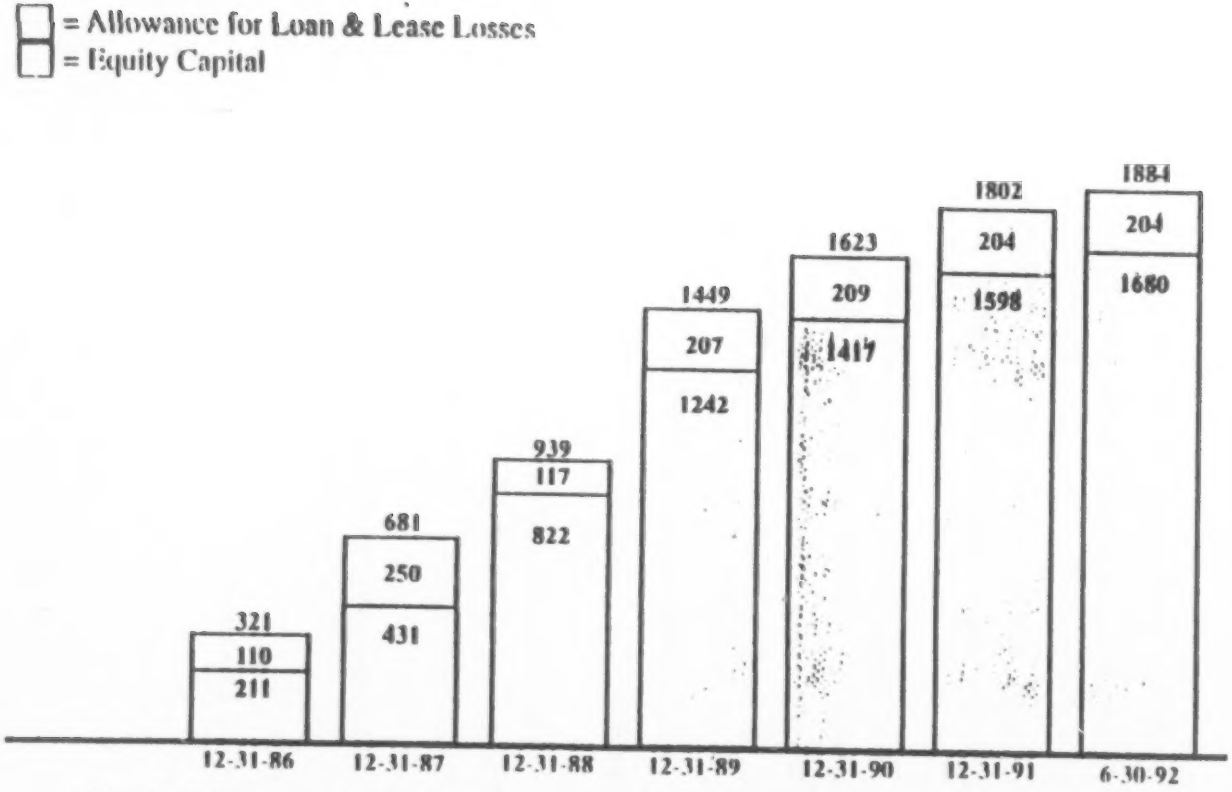
The suggestion for en banc rehearing has been circulated to the full court, and no judge of the court has requested a vote on the suggestion for rehearing en banc. Fed. R. App. P. 34(b).

The petition for rehearing is DENIED, and the suggestion for a rehearing en banc is REJECTED.

The order of the district court filed September 13, 1995 staying the sale of the First National Bank & Trust, Wibaux, Montana, is vacated and the stay is dissolved.

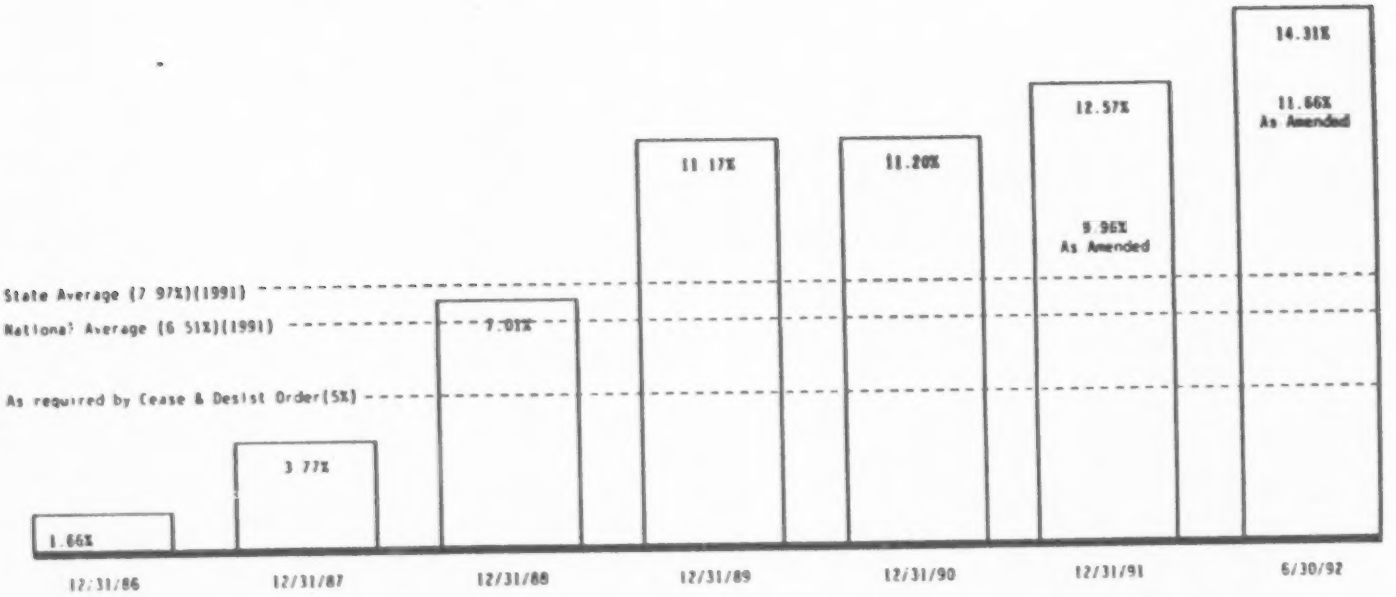
The mandate in this case shall issue immediately.

End of Document



Capital Accounts (Equity Capital) of The First National Bank & Trust

(In Thousands of Dollars)



CAPITAL RATIOS (EQUITY CAPITAL) OF THE FIRST NATIONAL BANK & TRUST

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MONTANA
BILLINGS DIVISION

FIRST NATIONAL BANK & TRUST, WIBAUX, MONTANA, and ITS STOCKHOLDERS, Thomas E. Towe Trust, Karen James Trust, Kristin Hartley Trust, Sara Horsfall Trust, Andrew C. Towe Trust, Grant Investments Fund, Irene Koch, and Dorothy Tow,	)	Cause No. CV 92-121-BLG-RWA
Plaintiffs,	)	Judge Jack D. Shanstrom
vs.	)	
THE COMPTROLLER OF CURRENCY,	)	**AFFIDAVIT**
Defendant.	)	

STATE OF MONTANA)
) ss.
County of Yellowstone)

I, THOMAS E. TOWE, being first duly affirmed,

depose and state that:

1. I am the Chairman of the Board of the First National Bank & Trust, Wibaux, Montana. I am also counsel for Plaintiffs herein.

2. Sheshunoff is an information service company that reviews and compares the published financial statements of all banks in the United States. On a periodic basis, it prints the results of its compilations. Attached as Exhibit A to this Affidavit is that portion of the 1992 compilation that includes the capital adequacy of all banks in the State of Montana. As can be seen from the exhibit, only seven banks (excluding First Trust Company of Montana which is a trust company, not a bank - it makes no loans) have a higher core capital ratio to total assets than the First National Bank & Trust, Wibaux, Montana. They are (1) Yellowstone Bank of Columbus, (2) Belt Valley Bank of Belt, (3) Yellowstone Bank of Billings, (4) Farmers State Bank of Denton, (5) Yellowstone Bank of Absarokee, (6) First Valley Bank of Seeley Lake, and (7) Big Sky Western Bank of Big Sky. All of these banks are located in the Western half of the State of Montana - West of Billings, Montana. Additionally, only four banks on the entire state have a higher risk adjusted capital ratio. (See the last column under capital ratios.)

3. The Plaintiff has engaged the services of H. O. "Burt" Price, one of the nation's foremost experts in bank regulation and examination. Among other things, he worked for the Office of the Comptroller of the Currency

for 31 years, from 1950 through 1981. He was commissioned as a national bank examiner in 1956 and appointed Senior Examiner in 1970. He received the Senior National Bank Examiner title, one of 25 in the United States, given only to examiners who have "demonstrated leadership and effective execution of the most difficult and demanding assignments, with a documented record of exemplary performance as a national bank examiner. He was also given a special award for consistently upholding high ideals of the OCC. He also received the Albert Gallatin award, the highest Department of Treasury career service award. A copy of his background and qualifications is attached hereto as Exhibit B.

4. Plaintiff has requested its expert, H. O. "Burt" Price, to review the decision of the Comptroller, the Plaintiff's Statement of Facts Which Establish A Genuine Issue of Material Fact outlining the Plaintiff's response to 49 contentions that are erroneous in this case, and the Affidavit and documents supporting those answers, and has indicated his conclusions regarding the significant contentions of the Defendant. A more detailed report will be provided in due course. A copy of his preliminary report containing some of his essential conclusions is contained in two letters which are attached hereto as Exhibit C.

5. Attached hereto as Exhibit D is a Report of Condition of the First National Bank & Trust, Wibaux, Montana, as of June 30, 1992, just five days after the appointment of a conservator. To the best of my

knowledge, it accurately reflects the financial condition existing at the time of the takeover by the Defendant.

6. Exhibit E attached hereto is a copy of the Report of Condition of the Bank as of September 30, 1992. As can be seen from the notation at the bottom of the Report, it reflects the numbers after the condominiums on OREO were charged off. Even after the charge off of these OREO properties, the Bank maintained an equity capital of 11.89% and a primary capital of 13.71%, far above average. Based on the Sheshunoff comparison, it still would be the strongest bank in Eastern Montana, and only seven banks in the entire state would be stronger based in equity capital (core capital).

7. The letter attached hereto as Exhibit F was sent by me to Kyle Cox, Chief Examiner for the OCC on the last examination of the Wibaux Bank, on December 1, 1991. It outlines the position of the Bank with regard to affiliated organizations under 12 U.S.C. § 221a(b) which contains a definition of "affiliates" which is essentially the same as 12 U.S.C. § 371(c) and 12 U.S.C. § 371(c)-1.

8. The letter attached hereto as Exhibit G was sent to me by Ralph E. Sharpe, Director, Enforcement & Compliance Division, OCC, on July 11, 1988.

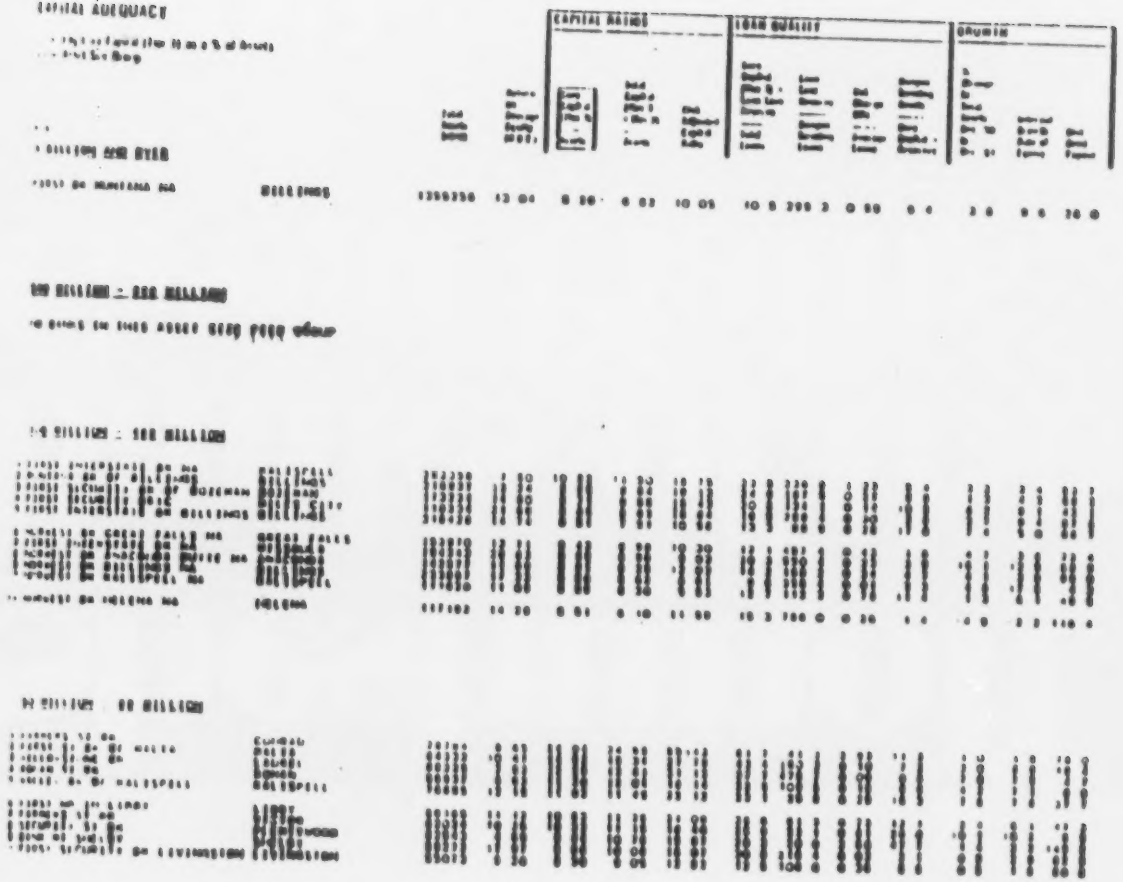
DATED this 8th day of December, 1992.

/s/THOMAS E. TOWE

AFFIRMED AND SUBSCRIBED before me this 8th day of December, 1992.

/s/ Martha M. Pruitt
Notary Public for the State of Montana
Residing at Billings, MT
(SEAL) My Commission expires: Jan. 18, 1994

EXHIBIT A



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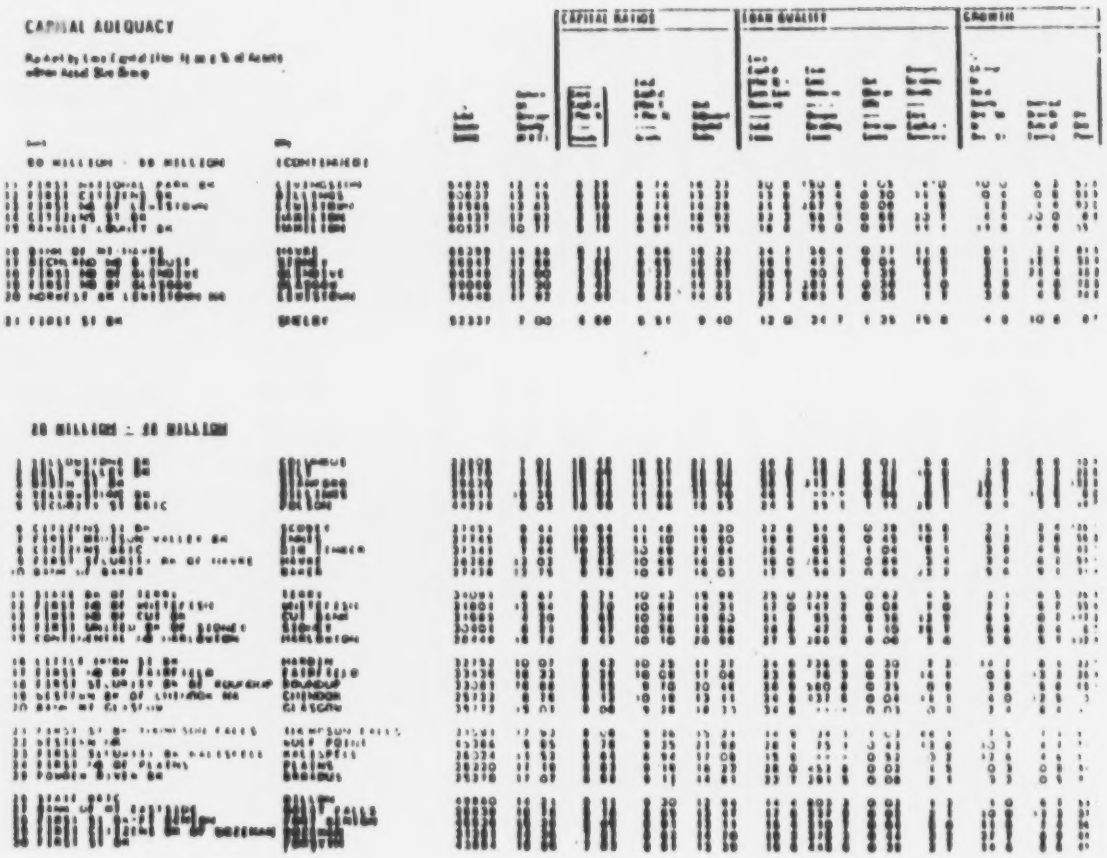
CAPITAL ADEQUACY
CAPITAL RATIOS
LOAN QUALITY
GROWTH
$0 MILLION - $0 MILLION
(CONTINUED)
$0 MILLION - $0 MILLION

BEST AVAIL

ABLE COPY

Exhibit B to Affidavit:

H.O. 'Burt' Price

Financial Consulting • Bank & Director Examination • Credit Review & Documentation

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13909 - 209th Ave. NE • Woodinville, WA 98072 • (206) 869-0607

QUALIFICATIONS SUMMARY

Over 40 years experience in banking including:

Credit Analysis, Review, Evaluation
Knowledge of Laws and Regulations for Bank Examination
Resident Supervision of Failing Banks
Management Evaluation
Asset-Liability Management
Adequacy of Reserve for Losses
Audit Management

WORK EXPERIENCE

Self Employed Bank Consultant 1986-1991

* Reviewed and graded loans in three banks where sales or mergers were contemplated.

* Reviewed loans in two banks for new management teams.

EXHIBIT B

* Continue to analyze loans and make recommendations at 7 banks.

* Evaluated files, graded loans, reworked management reports, and controls at a mortgage company.

* Evaluated mortgage loan packages for two investment trust companies. Review included ascertaining that Underwriting Criteria was met.

* Continue to conduct an annual Director's Examination.

Peoples National Bank, Seattle, WA 1981-1986
Vice President and General Auditor

* Managed auditing department of six areas: Correspondent Bank Examinations, Corporate Audits, Credit Examinations, Trust Audits; E.D.P. Audits, Special Investigations.
* Reported results directly to the Examining Committee of the Board of Directors.
* Revised procedures and developed new report formats.
* Prepared budgets; kept expenses within budget.
* Interviewed job applicants, trained and counseled staff of 22 - 30 employees.

Office of the Comptroller of the Currency, Department of Treasury
Minneapolis, Duluth, Helena and Seattle. 1950-1981

National Bank Examiner (Commissioned 1956, appointed Senior Examiner 1970)

* Examined over 60 banks in eleven midwestern, southern and western states including Alaska.
* Headed examinations of international branches in India, Indonesia, Japan, Korea, Malaysia and Thailand.
* Planned, Organized, conducted examinations, evaluated credits of complex problem banks and larger regional banks.
* Submitted recommendations and consulted with Senior Bank Management and Board of Directors.
* Evaluated work performance, provided counseling and recommendations for various personnel actions for the Seattle office.
* Special assignments included Washington, D.C. management training, on site (up to three months) supervision of specific failing banks, task force member and instructor for new examination procedures, and temporary duty with Federal Credit Union Examiners.

State Bank of Madison, Madison, Minnesota 1946-1950

* Involved in overall bank operations.

SPECIAL AWARDS

* Received Senior National Bank Examiner title, one of 25 in U.S., given only to examiners who

have "demonstrated leadership and effective execution of the most difficult and demanding assignments" with a documented record of exemplary performance as a National Bank Examiner.

* Given special award for consistently upholding high ideals of the O.C.C.
* Received the Albert Gallatin Aware, the highest Department of Treasury career service award.

COMMUNITY

* Conference faculty member for Assembly of Bank Directors, 1979.
* Speaker and panelist for Washington Bankers Association and other professional organizations.
* Authored articles for banking publications.
* Served two three-year terms on church council (President)
* U.S. Soccer Referee: officiated high school, college and adult games, 1976-1985. Treasurer, Washington State Soccer Referee Association, 1982-1986.
* Member Financial Advisory Committee Church, 1987-1991
* President Eastside Chapter National Association of Federal Retired Employees.
* Member Design Review Board Bear Creek Homeowners Ass'n. (Private Golf Club Community), 1990-1991

EDUCATION

Graduate School of Banking
University of Wisconsin, Madison, WI
- Completed 3 year program, 1961

LaSalle Extension University, Chicago, IL
- Basic Accounting Certificate, 1950

Continuing Education
- AIB Courses
- OCC Seminars (Interagency Banking School, International Banking School, Bank Fraud, Management, Advance Management).

PERSONAL

Married, three grown children.
Active in golf, swimming, fishing, hunting.

Exhibit C to Affidavit: (2 letters from H. O. "Burt" Price)

H.O. 'Burt' Price

Financial Consulting • Bank & Director Examination • Credit Review & Documentation

13909 - 209th Ave. NE • Woodinville, WA 98072 • (206) 869-0607

December 3, 1992

Mr. Thomas E. Towe
Attorney at Law
P. O. Box 30457
Billings, Montana 59107-0457

Dear Mr. Towe:

I have reviewed the Plaintiffs's Statement of Facts Which Establish a Genuine Issue of Material Fact" and an updated affidavit of Edward Towe, plus previous documents. I have not seen internal bank records to support these facts and thus my conclusion are based on information contained in the affidavits.

Comments on Cause No. CV 92-121-BLG-RWA

PLAINTIFFS' STATEMENT OF FACTS WHICH ESTABLISH A GENUINE ISSUE OF MATERIAL FACT.

EXHIBIT C

DEFENDANT'S CONTENTION

Grant Investments is a financial institution with a financial institution and that it has "no physical existence apart from the Bank" etc.

7. Pages 4-5 & 6. During my thirty plus years with the Office of the Comptroller of the Currency I examined numerous banks where the President of a Bank (both active and inactive) operated an office in the back room of a Bank. I have not seen this practice criticized.

DEFENDANT'S CONTENTION

The Bank's accommodations and indemnification of Grant Investments have resulted in sham transactions and substantial direct losses to this small bank.

10. Page 9. Based on the information I have it does not appear that the First National Bank of Wibaux, Montana has suffered substantial direct losses.

DEFENDANT'S CONTENTION

The claim that this transaction exposed the Bank to significant losses and, therefore, was an unsafe and unsound practice.

11. Page 11. It is standard banking practice to allow depositors to cover checks on the day presented. During this period there is no exposure to bank.

DEFENDANT'S CONTENTION

The "Jacobson" transaction was a sham transaction which resulted in the Bank constructing false records.

12. Pages 12-15. It is not unusual for banks and mortgage companies to date documents and not post or book them on the same date. Often times, on a construction loan for example, the first advance may not occur for a month and at that time the note is posted and starts accruing interest.

DEFENDANT'S CONTENTION

The Bank indemnified Grant Investments against losses on loans made by Grant Investments to David Preiss which was an "unsafe and unsound practice" which "resulted in substantial losses to the Bank, and represents the misuse of insured deposits".

13. Page 15. Under standard banking practices the bank could have advanced money to protect its interest. By advancing the funds bank would have assumed all the additional risk. When Grant Investments made the advance under a "LIFO" agreement it was to the banks advantage.

DEFENDANT'S CONTENTION

The Bank and Grant Investments has no oral agreement for the Bank to pay off the Zeimer & Epperson loan to Grant Investments upon the sale of the collateral. The Bank was not obligated to pay $8,548.36.

14. Pages 16-17. The Contract for Deed indicated

repairs had to be made and the agreement reportedly committed additional advances not to exceed $15,000. I see nothing illegal in participating the $8,038.58 to Grant Investments Fund and it is a common practice to pay off participants prior to bank unless this resulted in additional loss to selling bank. The participation should have been signed but since the funds were advanced by Grant Investments Fund, which was to the bank's benefit, the final result was the same as if the bank had not participated the loan.

DEFENDANT'S CONTENTION

The Bank failed to write down the value of Hlebechuk and Doeden properties thereby resulting in inaccurate call reports relating to OREO.

15. Page 22. I do not feel an appraisal which states in part that the appraiser could not appraise the contracts is acceptable. Contract balances were generally the maximum value banks were allowed to book rather than appraised value on O.R.E.O. I also feel the Bank is entitled to an answer on why the OCC did not follow up on their letter of February 21, 1990 asking the Bank to refrain from the proposed sale.

DEFENDANT'S CONTENTION

The Rasmuson appraisal represents a reasonable estimate of value of the properties in controversy at the time of the appraisal and at the current time.

19. Page 27. (Also see comment under 15) The sale of one of the units for $35,000 cash, plus cash generation of over $180,000 supports the contention that the appraisal was not acceptable and was in fact "beyond the scope of the appraiser" as stated in the appraisal.

DEFENDANT'S CONTENTION

The Bank relinquished control of a substantial amount of Bank assets and transferred them to Edward Towe which resulted in the Bank concealing "OREO expenses" and making "of-the-book's loans". This same account is also called a "slush fund".

21. Page 28. It is not unusual for bank's to use a subaccount such as this as long as the account is taken into consideration in Call Reports.

DEFENDANT'S CONTENTION

The Bank has continually relied upon an appraisal dated December 4, 1985, for the Beggers Diamond V. Ranch loan.

27. Page 36. This is not a required nor standard banking practice. I have never seen a request for an updated appraisal on an FHA guaranteed loan which is performing.

DEFENDANT'S CONTENTION

The decrease in the Nistler loan was $6,300 less than projected by the Bank.

28. Page 36. If documented in credit file as stated I do not feel defendant's contention is valid.

DEFENDANT'S CONTENTION

No monthly payments were made by Peters for November 1990, January 31, 1991, March 1991, and April 1991, and therefore the workout plan is not in compliance even though the Bank reported that the plan was being complied with.

30. Page 37. The four prepayments should be taken into consideration and loan considered current under normal banking practice.

DEFENDANT'S CONTENTION

The Peters loan has reduced only $1,063 in 19 months and will be $1,800 short of full payment when the 17 additional monthly payments are applied.

31. Page 38. Comments indicate additional funds were advanced and documented as required by the Cease and Desist Order and thus not a valid contention.

DEFENDANT'S CONTENTION

The Inklebarger loan has been reduced by only $554 in a 23 month period, thereby implying that the borrower is not complying with his workout plan as stated.

32. Page 38. It appears an error was made by not taking into account that the payments quoted only represented 10% of reduction. Since

borrower had never missed a payment the Defendant's Contention is incorrect.

REGARDING STATEMENTS BY EDWARD TOWE

Items 19, 21, 22, 25, 26, 36, 37, 38, 42, 44 and 50 are commented upon on pages 1 through 3 of this letter.

DEFENDANT'S CONTENTION
The reduction from August 1, 1988, to May 31, 1992, was $968.

29. Page 37. My experience as an examiner in agricultural credits supports bank's contention that one examination was at a low point and the other at a high and this fact should have been taken into consideration. Also the additional purchases should have been considered in analyzing the credit.

DEFENDANT'S CONTENTION
Lanny Peters did not pay stipulated payments for November 1990 and January, March and April in 1991.

30. Provided the statement by Edward Towe is correct on the four advance payments the loan was not properly reviewed and criticism of this credit not warranted.

COMMENTS REGARDING OTHER MATTERS CONTAINED IN OTHER DOCUMENTS:

The Bank was criticized for not having income tax returns or failing to have same signed. I have seen nothing in regulations which require this, and while I agree it is prudent, I have not seen this criticized in other banks.

Even with these tax return exceptions, which had never previously been criticized, documentation exceptions decreased from 90% to 40% at the latest examination in 1992. This does not support contention that bank was not showing improvement.

At the last examination the bank was assigned a Camel 4 rating "high potential for failure, but not yet eminent or pronounced". Since no examination was conducted in the interim I fail to see what circumstances changed to warrant action taken.

Contentions not commented upon are either legal questions or those on which I lack information to make a statement.

Should you have any questions on this letter or other matters doe not hesitate to contact me.

Sincerely yours,

s/s H. O. Price

H.O. 'Burt' Price

Financial Consulting • Bank & Director Examination • Credit Review & Documentation

13909 - 209th Ave. NE • Woodinville, WA 98072 • (206) 869-0607

December 7, 1992

Mr. Thomas E. Towe
Attorney at Law
P. O. Box 30457
Billings, Montana 59107-0457

Dear Mr. Towe:

Comments on Cause No. CV92-121-BLG-RWA

Supplement to letter of December 3, 1992.

PLAINTIFFS' STATEMENT OF FACTS WHICH ESTABLISH A GENUINE ISSUE OF MATERIAL FACT.

DEFENDANT'S CONTENTION
Bank failed to place delinquent loans on nonaccrual and Board minutes did not reflect proper review:

36. Page 43. Standard bank policy is to place all loans delinquent in excess of 90 days on nonaccrual, unless loan is well secured and in the process of collection. Providing

loans met this criteria bank should not be criticized.

It is standard bank practice to present a list of delinquent loans to the Loan Committee prior to full Board Meeting. The full Board normally then refers to this list without commenting on each name.

DEFENDANT'S CONTENTION
Loans were made before any credit information or financial statements were obtained.

39. Page 46. Dating papers at the time of application is a common practice as commented upon in my prior letter of December 3, 1992, page 2, item 12. Providing this criticism refers only to Condominium loans the bank should not be criticized for this practice.

DEFENDANT'S CONTENTION
In part "the existance of credit and collateral exceptions constitutes a failure to adhere to bank policy."

33. Page 39 of President Edward Towe's response. I agree no bank can realistically eliminate all credit and collateral exceptions.

See page 5 of my December 3, 1992 letter for comment regarding failure to obtain tax returns.

Edward Towe's contention Item 46 Page 50.

In part "The motel loan referred to on page 122

of the Decision was participated by the Bank to a bank in Glasgow, who in turn, transferred its interest to Grant Investments Fund. Under this agreement the Bank retained the primary responsibility for collecting the loan in the event of default."

Most participations contain this language and thus the bank's action was normal banking procedure.

Sincerely,

/s/ H. O. Price

UNITED STATES OF AMERICA - OFFICE OF THE TREASURER - OFFICE OF THE COMPTROLLER OF THE CURRENCY
IN THE MATTER OF TOWE
CAUSE NUMBERS OCC-AA-EC-93-42 & OCC-AA-EC-93-43
TRANSCRIPT OF PROCEEDINGS (VOL. XXX)
DATED AUGUST 14, 1995

Testimony of H. O. "Burt" Price

Q. (By Mr. Towe) Mr. Price, based on all of the information available to you and that you have reviewed in this case, have you formed an opinion as to whether or not the OCC was justified as to the sufficiency of the facts to remove Ed Towe for life?

MR. SAVOY: Objection, Your Honor. Calls for a legal conclusion.

JUDGE SHIPE: Denied.

THE WITNESS: Yes.

Q. (By Mr. Towe) What is that opinion?

A. I feel the OCC was not justified.

Q. And have you formed an opinion based on all the information available to you as to whether or not the OCC was justified in sufficient facts to remove Thomas Towe for life?

A. Yes.

Q. And what is that opinion?

MR. SAVOY: Objection, Your Honor.

Calls for a legal conclusion.
JUDGE SHIPE: Denied.
THE WITNESS: No.
Q. (By Mr. Towe) And have you formed

an opinion, based on all the information available to you, whether there are sufficient facts to justify the seeking of civil money penalties against Edward Towe?
A. Yes.
Q. What is that opinion?
MR. SAVOY: Objection, Your Honor. Calls for a legal conclusion.
JUDGE SHIPE: Denied.
THE WITNESS: No.
Q. (By Mr. Towe) Based on all the information available to you, have you formed an opinion as to whether or not there are sufficient facts to justify seeking civil money penalties against Thomas Towe?
A. Yes.
Q. And what is that opinion?
A. No.
MR. SAVOY: Objection, Your Honor. Calls for a legal opinion.
JUDGE SHIPE: Denied.
Q. (By Mr. Towe) And your answer?
A. No.
Q. Now, I want to ask you to explain the reasons for your opinion. The first question I

asked was whether there was sufficient facts to justify removing Edward Towe for life.

What are the reasons for your conclusion or opinion?

A. Because, number one, the OCC in Washington always stated that the field examiners were their eyes and ears, and all decisions in Washington, D. C. were based on what the eyes and ears, in other words the field examiner, the information that was given by them. And in the Wibaux Bank exam, I do not feel that many of the facts were documented; comments didn't represent factual, typical or normal criticisms.

Q. Okay. And --

MR. SAVOY: Your Honor, may I ask is the witness referring to a document during his testimony?

THE WITNESS: No, I am referring to some of my notes to refresh my memory.

Excuse me. That was a question to counsel, I'm sorry.

MR. SAVOY: May we be provided with a copy of those notes, Counsel?

THE WITNESS: They're messy.

MR. TOWE: Take a look at them.

MR. SAVOY: I would like to make a

copy of them.
MR. TOWE: All right.
JUDGE SHIPE: Can we continue while a copy is being made of those notes?
MR. TOWE: I would prefer that we wait until he gets his notes so he doesn't make any mistakes.
JUDGE SHIPE: All right, we will be off the record for a moment.
(Off the record.)
JUDGE SHIPE: We will be back on the record.
Mr. Towe, you may continue.
MR. TOWE: Thank you.
Q. (By Mr. Towe) I believe we were at the first reason as a basis for your opinion, and I think you indicated in addition to the fact that the Comptroller were the eyes and ears of the examiners (sic), the criticisms were not well documented and were not normal in the standards.
Now, was there something else in that first reason you wanted to explain?

A. Yes, I think that leaving out the facts that are disputed or were disputed in the case which I disagreed with, that the legitimate facts remaining didn't support the conclusions reached.
Q. Now, is that reason also a reason for

your second opinion, which was the facts did not justify the removal of Thomas Towe for life?

A. Yes.

Q. Was that reason also a reason for your third and fourth opinion; namely, that the facts did not justify seeking civil money penalties against Edward Towe and Thomas Towe?

A. Yes.

Q. And both opinions?

A. Yes.

Q. Is there a second reason?

A. Yes. To support this, I feel that management received little credit for improvement shown as supported by the figures that I have the following figures.

In 1989 examination, had 90% financial statement exceptions. The '91 had 40% financial statement exceptions.

Collateral exceptions for 54% in '89.

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They were reduced to '91 -- or to 26% in '91.

Credit exceptions in the 1989 examination totaled 131. In the '91 examination, they totaled 3.

Collateral exceptions were '59 in the '89 report. In the '91, they had decreased to 16 exceptions.

Q. And what do all those facts show us?

A. It doesn't support the conclusions that the bank was going the wrong direction or failing. There was improvement shown. In fact, I think the examiner in many of areas in his comments did indicate that there was some improvement shown.

Q. Were there other improvements that you wish to refer to in reason number two?

A. Well, looking at the conditions, again, when Ed Towe took over the bank, the current and the situation in '91, in 1987, which is prior, but it was when he first took over, the capital of the bank was 211 million (sic).

In 1991, when the conservatorship was appointed, the capital had increased 1,884,000.

Capital equity in 1987 was 1.66. In 1991, it was the tenth highest in the state out

of 143, and I took that out of a Sheshu --

Q. Sheshunoff?

A. Sheshunoff report, thank you.

In '87, when the bank was taken over by present management, there were 10 houses in Other Real Estate Owned that had been foreclosed upon. In 1991, all of these were out.

There were 28 mobile homes in Other Personal Property Repossessions. All of these have been paid off or out.

One farm was in the bank; it is gone. Two apartment houses, which later condoed.

For further information, that's been covered pretty well in the report, and I won't go into that, but they are out.

One motel was in Other Real Estate Owned. It was sold without loss to the bank. The bar which was in trouble is, Grant has purchased.

Yet, in spite of all these things, poor assets being eliminated, the capital increased as indicated.

Q. And how about did you have any other evidence of improvement that you wanted to relate in this particular area, reason two?

A. Well, I think that I stated that none of this improvement was ever mentioned - well, little credit was given for the improvement to support these figures.

Q. Which is your basic reason?

A. Yes.

Q. What about earnings, did you want to say something about earnings?

A. Earnings had improved. And I think I commented on that, but I failed in my notes to show earnings. The earnings had improved, though, considerably.

Q. And how about the classified assets?

A. It had decreased considerably.

Q. Now, is this reason two also a reason

to support your opinion that the facts do not justify removal of Thomas Towe for life?

A. Yes.

Q. Does this reason, the second reason, also support your opinion the facts do not justify the seeking of civil money penalties against Edward Towe and Thomas Towe?

A. Yes.

Q. Is there a third reason?

A. Yes.

Q. What is that?

A. The CAMEL 4 rating. In my 30 years with the OCC and my 10 years as a banking consultant, I have never seen or heard of a CAMEL 4 being taken over or CMP charges on a CAMEL 4 bank.

Q. Or removal?

A. Removal, the action taken in this case.

Q. And does that same reason apply to all four of the opinions that you gave earlier?

A. Yes.

Q. Is there a fourth reason?

A. Yes.

Q. What is that?

A. The problems in this case originated with previous management, and the C & D was also issued to previous management.

With the improvement shown that I have evidenced under the present management,

again I have never seen action like this taken.
I go back to total improvement, and again where I've testified, you know, and the improvement that I pointed out, and these are taken from the OCC Examination Reports, and

other -- looking at the financial statements of the bank, I reached this conclusion.

Q. Is that -- have you completed all that you wanted to say on reason four?

A. Yes.

Q. And does the same reasoning, the same reason also apply to all four opinions that you gave?

A. Yes.

Q. Is there a fifth reason?

A. Yes, because to me, there was an apparent lessening of concern by the OCC over this period of time, for example, less frequent examination. This usually is an indication to bankers that improvement is being shown.

'88 to '92, back in '88, the bank was being examined every six months. In '92, it had been two years. And I can understand because I feel I have knowledge of how bankers feel, that the Wibaux Bank and the Board might have relaxed a little bit thinking that they were doing okay.

Q. And does that reason apply to all four of your opinions?

A. Yes.

Q. Is there a sixth reason?
A. Yes.
Q. And what is that?
A. The condos were inherited from the previous management. There were serious problems. Management recognized these problems and used creative financing in an attempt to work out of their problems.
And given the circumstances at that time, this was probably the only way of getting out of the problem and still saving the bank. Hindsight indicates that this creative financing, if continued, would have provided satisfactory results.
Q. And in that connection, can you say anything with regard to the extension requirement, the five-year extension -- or I mean the five-year requirement that OREO be sold within five years?
A. In the banks I have worked with and as an examiner and since then, I have seen. numerous instances where if some attempt was made, and it was not feasible to dispose of the property where extensions of the five years were granted by the Office of the Comptroller

of the Currency.

Q. Now, I --

A. Excuse me, may I continue?

Also, on the Rasmuson appraisal -- no, I guess that was a separate one. Go ahead.

Q. And do you think an extension should have been granted in this case?

A. It was standard practice. I don't know, I can't recall in my 31 years where it was never not extended, and I did have those situations.

Q. Now calling your attention to the appraisal as it relates to the condominiums, can you say something with regard to the OCC's position on the appraisals?

A. I feel that the 3/16/88 Rasmuson appraisal was flawed due to the qualified opinion, which to me was unacceptable and should not have been insisted upon as used.

Q. Could you --

A. And I also take exception to saying that he was not qualified to base any of the appraisal on the contract balances.

In every appraisal I have seen where there are contract balances where the property

has been sold, this is a consideration. And to me, the mere fact that he brought it up and mentioned them indicates that it is a consideration in real estate appraisals, yet he

stated he was not qualified.

Q. Just to clarify, the qualification that Mr. Rasmuson put in his appraisal that you refer to is what, can you explain that qualification?

A. I can't use the exact terms, but he did state these were not used because he was not qualified to give an opinion, or something to that effect.

Q. These were the contracts?

A. The contracts, yes.

Not within the scope of his -- I think those were his terms, not within the scope of his expertise -- he didn't say "expertise"; I considered it expertise -- of his knowledge, or something to that effect.

Q. Was there anything else in the Rasmuson -- the correspondence regarding the Rasmuson appraisal that you wanted to comment on? And let me call your attention to the reference to Mr. Quade.

A. Oh, yes.

I also -- I'm not -- I do not understand, and someplace I have got the number of that exhibit of Mr. Quade's - or not the exhibit, it is a --

Q. I believe it is a letter that was entered as an exhibit?

A. It was a letter entered as an exhibit,

and it did cite a Banking Circular or Bulletin, and it cited a number in which -- no, excuse me I'm thinking of something.

Okay, let's go back to Mr. Quade. There is correspondence in there indicating that Rasmuson contacted the Billings office and requested the examiner in charge. However, the correspondence was from Mr. Quade, and he indicated that a cost approach should be used in that appraisal. And I have -- I feel this was a little bit beyond the scope for an examiner to make this recommendation.

Q. Do you think it was accurate, the instruction that Mr. Quade gave Mr. Rasmuson?

A. In my opinion, no, because of the complex appraisal and the situation.

Q. Now, calling your attention to the condominium problem as a whole, can you tell

me what you think the OCC should have done in connection with this problem?

A. Would you repeat that, Tom.

Q. Have you some thoughts as to what you would have done or the OCC should have done in this connection?

A. Well, I think --

MR. SAVOY: Your Honor, I'm going to object for the record. I believe it is clear during his earlier testimony that he did not

review all of facts in this case, and I don't think he is qualified to form an opinion as to what the OCC should have done. It's totally speculation on his part given the fact that he admits he hasn't reviewed all of the facts.

JUDGE SHIPE: Denied.

THE WITNESS: Okay, the question was, I believe, Tom, a little different than the objection. You asked what I would have done, not the OCC, as a field examiner.

And as a field examiner in those days, I would have probably worked with the bank a little harder. My recommendation would probably be, under the circumstances and what they had done, and even though the improve-

ment was slight, it was some improvement, I would have recommended an extension over the five-year period.

Q. (By Mr. Towe) All right.

Does the reason you gave as the sixth reason apply to all four opinions that you gave earlier?

A. Yes.

Q. Is there a seventh reason?

A. Excuse me, I did find, that was Exhibit 641 which I couldn't find, which were Quade's was given in evidence, okay?

Q. Okay.

A. The seventh, yes.

Q. Could you give us the seventh reason for your opinions?

A. The report gave comments all the way through, and certainly gave the impression that Towe concealed, falsified records, diversion of funds, schemes and so forth were used.

And I do not confer that this language was proper because there was trail, paper trails on all these transactions, which doesn't indicate to me it was concealed.

And when you divert funds, you don't

leave -- when you scheme to do something, you don't do it openly. And I feel that based upon the records that I saw and the Examination Reports, the records were there, paper trail records.

MR. SAVOY: May I object just for clarification.

He is referring to which Report of Examination, for the record?

Q. (By Mr. Towe) And which review of examination did you have reference to in that response?

A. Primarily I think the 1991 completed in '92.

I would also --

Q. By Mr. Cox?

A. By Mr. Cox.

I would also like to clarify in that

regard, when I refer to the '91 examination, in some of the correspondence, it refers to it as the '92. And in fact, that is one and the same examination, because it commenced in the fall of '91, but it was by completed in '92.

Q. Okay.

A. And I think some of the

correspondence and some of the letters I referred to, or figures, I cite '92 and then occasionally, it's '91; they are one and the same.

Q. And does this reason apply to all four of your opinions?

A. Yes.

Q. Is there an eighth reason for your opinion?

A. Yes.

Q. What is that?

A. I reviewed the 1991 ROSA and the '93 ROSA, and in my opinion, there is clearly evidence of bias.

As an examiner, I have reviewed over 500 examination records, and I feel competent to evaluate the contents.

The bank continued to be criticized in the '91 exam in areas showing improvement.

In '93 the Examination Report showed a change in attitude in that any improvement was applauded, even though less substantial than that shown in the '91 report.

And for that, I go back to my previous testimony that, for example, in, I believe the statement exceptions or collateral dropped by

100 the previous time, this time, they were the same number, and I have the figures on -- to support that.

The '93 examination's, the credit exceptions were reduced from 31 to 10. But the previous time, there was 100, a reduction 100 of criticized points.

Collateral exceptions were 59; 16 from '89 to '91. They remained at 16, yet the language was entirely different, even though it wasn't substantial or significant, and those were the terms used, "significant improvement". And I feel that this shows bias or prejudice.

Q. Were there other examples of that same thing in those two reports?

A. Yes. Page 1 of the '93 report on "Findings and Overall Conclusions", I quote from the Examination Report,

"The overall condition of the bank has improved significantly."

Again, this was not supported by my previous comment.

On Page 3,

"Paperwork bad, but

intent is okay."

Definitely a different attitude, because the intent, if it didn't produce the results under previous management was also considered an unsafe and unsound criticized condition.

Page 4, "Excuse the exception" -- I'm quoting again --

"Excuse the exemption due to untrained staff and stated most deficiencies are technical and easily corrected."

Again, this is a little different playing field than I observed in previous exams. Whether they were easily -- whether they were tech -- most of the problems were the same; they might have showed slight improvement, which was indicated in previous exams, but now the attitude was entirely different, "easily corrected", "technical".

Page 7, Article III, Partial Compliance. The examiner comments, I quote,

"The form includes sections if completed would

comply with the requirements of this

Article."

However -- now, this is mine again-- oh, now, I'm still quoting, excuse me.

"However, until his departure, executive VP Huether was completing the forms and omitting the same information that had been omitted previously."

Now this is a statement in there I quoted. Before Towe was personally blamed, and it was not acceptable, and it was repeated as an unsafe and a unsound -- it was considered AN unsafe and AN unsound practice.

Q. And was that done in '93, same criticism?

A. In '93, it was not.

And at that time -- and it goes on, or my is, previous management had requested the same information; they had chained the form, but they were blamed directly, management and director, rather than excused as it was in this one, which I think is a complete change in

attitude.

The examiner stated the same omission, but he reached an entirely different conclusion, which to me, indicates bias. And again we get back to this unsafe and unsound, which was the basis for a lot of this hearing.

Q. Have you finished with reason eight?
A. Yes.
Q. Does the information you gave us regarding the eighth reason apply equally to all four of your opinions that you earlier stated?
A. May I go back? There was one other issue in my notes here that I missed.
Q. All right, please do.
A. The exam in '91 -- okay, the past unsafe and unsound banking practices in almost all instances were eliminated in the '93 examination. Even though many of the things were repeated with little change, they remained in the report, but they were looked at, they were acceptable.
Again I just feel that was additional. It wasn't just in the instruments I mentioned, in other words, under III, the other -- the other Cease and Desist also had somewhat the

same language. And they also in previous examinations indicated some improvement, or slight improvement; now they were acceptable.
Q. As opposed to not being acceptable?
A. As opposed to not being unacceptable, and in several cases unsound and unsafe -- unsafe and unsound banking practices.
Q. Now, does the information you provided us under reason eight, the eighth reason, apply equally to all four of the opinions

you gave us earlier?
A. Yes.
Q. Is there a ninth reason?
A. Yes.
Q. What is that?
A. I feel alternative courses of action would have been more appropriate.
Q. Could you explain what some of those might be?
A. Number one, I feel they could have appointed a more senior examiner.
Q. Would you explain.
A. Well, in my career, and generally speaking, and I see this in the banks that I'm still doing that are operating under a Cease

and Desist, they send some senior examiners out with considerably more experience than what this particular examiner had who made this examination.
Q. And for example, are you familiar with how much experience this -- who are we talking about, what examiner?
A. Kyle Cox.
Q. Are you familiar with his experience?
A. Yes.
Q. And what is that?
A. I haven't looked at it in two years, but he worked in a bank, and he was -- prior bank experience and about five years with the

OCC.

Q. Are there other alternatives that you think would have been more appropriate?

A. Yes, I think that they could have used outside senior examiners where bias was claimed. And there's a precedent that was set in California where it determined that there wasn't any bias, and I have no way of knowing, but since it was done there, I have no reason to doubt but it might have been done in other cases too. But there was a precedent set in

California of sending in more senior people.

Q. To review the --

A. To review and see if there was any bias and see if the facts and so forth and the conclusions reached were supported in the working papers.

Q. And are there any other alternatives that you would look at?

A. Well, normally I see someone from the Region -- before this type of action is taken, I see someone from the Regional Administrator's Office or someone coming in and review it with management following the examination.

Q. And --

A. This had been done previously when the bank was in serious trouble.

Q. And it was not done at this time?

A. It was not done at this time. Again, inferring that things had improved.

Q. And is this something that would constitute a warning to the management, is that what you are referring to?

A. Yes.

Q. Are there any other alternatives that you would like to mention?

A. The C & D was issued many years before, and at that time, it addressed the apartment issue. This became somewhat a different issue in that these were now condominiums. And there was no mention of the condominium at all in that original C & D.

It did not cover any conflict of interest or affiliations and so forth, which to me, at the time it was closed, were major issues. So I think the new C & D might have been issued prior to the CMP and the conservatorship being appointed.

Q. Now, you just mentioned prior to it being closed. You didn't mean closed, did you?

A. No, prior to the conservative -- the takeover, okay.

Q. And does this reason apply equally to all four of the opinions you gave earlier?

A. Yes.

Q. Is there a tenth reason?

A. Yes.

I do not feel that the bank was treated

fairly and in an unprejudiced manner. And the first -- the first reason is I think Quade should not have appointed himself to do this

examination, and I feel that once the OCC became aware of this fact, they should have purged this exam from the ROSA and the SMS, because it does influence, it is a starting point for all future examinations, and it would influence the examiner following.

Q. Are there other items that you would like to refer to in your tenth reason that the bank was not treated fairly and in an unprejudiced manner?

A. Private loans from the bank is not uncommon practice, and I haven't seen it criticized indeed this manner, so I feel it is unfair treatment.

Q. And you are referring to the loans that were made by Grant Investments Fund?

A. Loans made in the so-called back room.

Q. And you have run into that practice in the past?

A. Yes, numerous times.

Q. Are there other items that you would like to refer to as causing you to believe the bank was not treated fairly and in an unprejudiced manner?

A. I don't think that the bottom line

analysis was properly used.

I'll go back to the new examination procedures, which was also quite a while ago, but at that time, an examination changed from what was called a snapshot to looking at the facts.

And at that time, the Controller of the Currency, James Smith, in his opening remarks to our group, stated that in the future, examiners would not go in and take this snapshot picture. They would go in and, and he compared it to a match factory, where you didn't check all the machinery; you didn't see whether there was a loose wheel somewheres or anything else. You went to the boxes of matches, the final product, and if they all lit, you didn't worry about the details.

In other words, at that time, and I think today it still continues, that the bottom line is a very important item, and this was totally ignored. Well, maybe not totally ignored, but ignored.

Q. Now, I have been asked --

A. This indicates bias to me.

Q. And I have been asking you about

this when you say the bank was not treated fairly or in an unprejudiced manner, are you

referring to Edward Towe and Thomas Towe, the Respondents herein this case?

A. Yes.

Q. Are there other items under this category?

A. Loans were criticized in the report after it was paid.

At the time, I was a junior examiner in Duluth, I did this on one bank, and I got a call from the Regional Office and said you can't do this; it is not proper. If the loan's paid, it couldn't have been that bad, I don't care how you feel about it.

And I have never seen that -- I have never seen loans in any of the banks subsequent to being examined where a loan has been written up after it has been paid.

Q. And was that done in this case?

A. Yes.

Q. In more than one occasion?

A. In two occasions that I recall.

Q. Are there other items under this category?

A. In the report, there was a noncompliance for with Banking Circular 115, which stated that it was -- that Florence Towe's services should be reviewed on a monthly basis.

I have seen a lot of this type employee, and their services are reviewed, but

never seen a request to do it on a monthly basis.

Q. Are there other items you would like to bring up in connection with the unfairness to Edward and Thomas Towe and the lack of -- or that they were treated in a -- not treated in an unprejudiced manner?

A. Director loans and payments to E.T., Towe appeared reasonable. And again, I'm going back to I saw nothing that was significant that hurt the bottom line of the bank.

Q. Now, are you referring to the monies that were paid to Edward Towe?

A. As salary or indirect salary, or I think he had one small loan that was in there as a result of some transaction.

Q. And what you are saying is that --

A. I did not view those improper, yet they were highly criticized in this instance.

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Q. Are there any other evidences of unfairness?

A. Thomas E. Towe was the only director singled out for civil money penalties. And I failed -- I cannot understand how we can single out one director, when to me, directors have always been able to delegate authority, but never responsibility. The responsibility ultimately always lies with the director.

And so even though maybe Ed was

appointed as an attorney, and if that's how some of this came up, the responsibility still is with all the directors, so I feel this is prejudice to single out one director.

Q. You mentioned that Ed was appointed as an attorney --

A. Excuse me, Tom appointed as an attorney.

Q. Okay.

And are there other items of unfairness that you would like to itemize here?

A. The report criticized Edward Towe for domination of the Board of Directors. In reality, I don't understand the criticism. This is true in any family bank I ever worked for or

ever been associated with or ever seen.

In family-owned bank, the controlling interest always dominates the Board. And thus, I don't really understand why this was made a major criticism.

Q. Now, you have listed eight different items of unfairness to Edward and Thomas Towe and reasons why they were not treated fairly or in an unprejudiced manner.

Are there other examples of bias in addition to these you've specifically mentioned?

A. Yes, there were numerous other -- there were numerous other pages in the Report of Examination, of the '91 Report of

Examination, where I made comment.

Q. Okay.

Now, do these reasons apply as a reason for all four of your opinions as you've stated earlier?

A. Yes.

Q. Is there an eleventh reason for your opinions?

A. Yes, again. And I'm quoting from an instruction of National Bank Examiner Handbook which is not currently in use, but I

still -- I think that the principle is still there, and since it is a prior one, but I think this situation fits somewhat.

And I'm quoting from the Handbook, and because it's a whole paragraph, I'm going to read all of it.

> "Some examiners are consistently able to achieve excellent results on their examinations. The technical competence of the examiner is partially responsible for consistent achievement, but of equal importance is the attitude of the examiner in his official dealings with bank

officers and personnel. An examiner of great technical competence can almost completely defeat his own efforts and injure the interest of the Controller's Office by a poorly considered attitude

in his relations with bank personnel. An examiner losses dignity, stature and respect when he makes any obvious attempt to impress upon a banker the extent of own importance and authority, particularly so when he seeks to achieve this by means of a domineering, caustic self-important or surly manner. Without exception, bankers resent officiousness, undue self-importance, sarcasm and a failure to exercise courtesy."

Some of the things -- I think this explains why some of the resentment, and again by the Controller at one time, his own words here, bankers resent this, and it does -- and I

really feel reading the reports, I can see much of this in those reports and the correspondence that I can relate directly to this quote.

Q. Are you referring to the attitude of Kyle Cox and Brian Quade?

A. Yes.

Q. And do you feel that these comments that you wrote -- I mean that you read apply to those situations?

A. I think that they were, to me, good examples of that quote.

Q. And does that apply equally as a reason for all four of your opinions?

A. Yes.

Q. Now, is there another twelfth reason for your opinions?

A. Yes.

As an examiner and as a consultant, I have worked with many banks who were in worse condition. They had less capital, poorer earnings, weaker management, management with poor prior records and not showing the percent of improvement as indicated in the Wibaux examination, and in none of these cases were a takeover or a removal considered.

Q. And do you remember that this is a further reason to support your opinions that removal is not appropriate in this case?

A. On the removal, yes.
Q. And does this apply equally to both Thomas Towe and Edward Towe?
A. On the removal, yes.
Q. Now, before continuing on, let me divert a moment and ask you a different question, and I want to come back to at least one more reason.
Have you ever seen separate subaccounts in banks for keeping track of income or expenses for a particular project?
A. Yes.
Q. And is that something that is a severe and serious problem to be criticized?
A. No.
Q. And are you familiar with the motel, the reference to the motel income and the condominium expense accounts, two separate accounts, that have been referred to by the examiners in this case?
A. Yes.
Q. And would you consider that the existence of those subaccounts was a matter of serious concern to the bank?
A. No.

Q. Okay, can I ask you if there are any other reasons to support your opinions that you

gave earlier?

A. Well, from everything I reviewed, I feel there is insufficient facts to support the removal and CMP.

Q. And can you explain?

A. Yes. There was no evidence of personal dishonesty, no evidence of action which significantly affected the safety and soundness of the bank, no evidence that the bank has or will suffer significant financial losses or damages, no action was taken which would have jeopardized depositor funds, no evidence that Tom Towe or Ed Towe received any inappropriate financial benefits.

In fact, in looking back, the bank gained from these transactions, and the Towe family has lost money on the majority of the transactions which were anticipated -- or which were criticized in the Examination Report. This is also true since the conservator was appointed.

(Conference between Mr. Towe and Mr. Murphy.)

UNITED STATES OF AMERICA - OFFICE OF THE TREASURER - OFFICE OF THE COMPTROLLER OF THE CURRENCY
IN THE MATTER OF TOWE
CAUSE NUMBERS OCC-AA-EC-93-42 & OCC-AA-EC-93-43
TR. OF PROCEEDINGS (VOL. XXVIII)
DATED AUGUST 10, 1995

Testimony of William Grant

Bill Grant.

WILLIAM GRANT,

having been first duly sworn to state the truth, the whole truth, and nothing but the truth, testified upon his oath as follows:

DIRECT EXAMINATION

BY MR. TOWE:

Q. Would you state your name and address for the Court, please.

A. My name is William Grant, and my address is P. O. Box 307 in Lovell, Wyoming.

Q. And Mr. Grant, right now, what is your present occupation?

A. I am a banker at the Bank of Lovell in Lovell, Wyoming.

Q. And what is your position with the bank?

A. I am the president and chief operating officer there.

Q. Could you explain just briefly what

your educational background is?
A. I received an undergraduate degree in business administration and economics from Jamestown College in Jamestown, N. Dakota, and did additional graduate worked at the

University of North Dakota and the University of Colorado.
Q. And have you also attended banking schools?
A. Yes, many banking schools and bank supervision schools provided by my employers of the time.
Q. And are you commissioned as a bank examiner?
A. I formally had held commissions with the Federal Reserve System. I had the FTC Commission designation accorded by the Office of Thrift Supervision, and was named by the Council of State Banking Supervisors as a senior bank examiner.
Q. And just briefly touching on your career, have you worked in savings and loans and bank organizations?
A. Yes, I have.
Q. For instance, can you just briefly state were you in a bank in North Dakota, or where did you start?
A. Well, I began my career in Jamestown, North Dakota at a small savings and loan in

1965.

Q. And then what happened next?

A. Well, I joined the, what was then the Federal Home Loan Bank Board as a junior examiner.

Q. And what year was that?

A. And that would have been 1967. And --

Q. And did you --

A. Go ahead.

Q. What did you do next?

A. Well, I went to work in Denver for First Federal Savings & Loan Association in Denver and was one of their bank -- their branch managers. I was an assistant vice-president there and was, later joined another savings and loan in Colorado, called Sheridan Savings, where I was vice-president and regional manager. I had four offices of that savings and loan.

Q. And what next?

A. I worked in Alaska as a vice-president of a bank and as a vice-president of First Federal Savings & Loan in Alaska. This was for a couple of years.

And then I came back and joined the Federal Home Loan Bank Board in, I believe it was 1979 in Seattle, where I began what

essentially was my examination, my career as an examiner.

Q. Before coming back did you work for the People's Bank in Alaska?

A. I did, yes. I was a vice-president of People's Bank, department manager, lender.

Q. And that was about, when did you come back then and start your career as an examiner?

A. I want to say it was 1979.

Q. And who did you work for at first?

A. I worked for District 12 of the Federal Home Loan Bank Board, which covered 13 western states, including, incidentally, Montana.

Q. And did that include examining savings and loan associations?

A. It did. I examined savings and loans associations at that time.

Q. Did you then manage a bank or a savings and loan for a short period of time?

A. I did. I was offered the opportunity to go open an office in Vail, Colorado, and I was there for about a year. We were profitable.

Q. And then what did you do?

A. I went to work for the Farm Credit Administration in St. Louis. There -- I was

there about five years, and became, I joined them as an examiner and was an examiner supervisor, something we called an activity manager. I examined the, at that time the

Farm Credit Banks, including Federal Land Banks, Federal Intermediate Credit Banks and banks for cooperatives in three districts, approximately 12 states.

Q. And then did you go back -- did you go to work for the Federal Reserve Bank?

A. Yes, I was recruited by the Federal Reserve System and worked as a senior examiner for the Federal Reserve Bank Chicago. I was a holding company examiner, but I also worked examining member banks there.

Q. And when did you come to Montana?

A. I came to Montana in the late 1980's, and I came to work on an agreement, a short-term agreement basis to fulfill a personnel need that they had. I came out for six months.

And at the end of that period, I went --

Q. What did you do while you were there?

A. I was a bank examiner. I was a Senior Grade 15, and I examined banks basically. I

was based in a Billings office and examined banks in eastern Montana.

Q. Then what?

A. Received an offer from the Federal Home Loan Bank of Pittsburg, very interesting situation, and I accepted and moved to Pennsylvania, based in the Philadelphia area,

where we were then the examining crews that were managed by the Federal Home Loan Bank of Pittsburg; were transferred to the Office of Thrift Supervision at the time when the Federal Home Loan Bank Board was melded into that new agency.

Q. And what was your function there?

A. I was a senior examiner out there. I was an examiner at a senior grade. I examined and was in charge of large, medium and small troubled thrifts, both in Pennsylvania, and on a limited basis I served national duty.

Q. And then did you return to Montana?

A. I did.

Q. And when was that?

A. 1990.

Q. And what --

A. 1990, I went to work for the State of

Montana again as a bank examiner, and I essentially was an examiner in charge, and I examined from the Billings office primarily and state chartered banks, including the largest banks currently state chartered at that time.

Q. And how long were you there?

A. A little over four years.

Q. And during the time when you were state examiner -- let's see, were you a senior examiner at the State?

A. Yes, considered a senior examiner

there. I was considered a senior examiner before I received the CSBS designation in Oklahoma.

Q. And CSBS?

A. Council of State Banking Supervisors.

Q. During your time as a senior examiner for the state of Montana, did you have an occasion to examine the bank in Wibaux, First National Bank & Trust?

A. Yes, I did.

Q. And when was that?

A. May, 1991. I was assigned to go to Wibaux and to determine the safety and soundness, the future prospects and other

conditions that were in the bank in Wibaux for the purpose of a conversion request, that is to say, a conversion request for a state charter that had been made by the Bank of Wibaux.

(Discussion off the record.)

MR. SAVOY: Tom, I have a clean copy with the exception of two words which are circled.

MR. MURPHY: That's fine, go ahead and use it.

Q. (By Mr. Towe) Handing you a copy of Exhibit R-16, do you recognize that document?

A. Yes. This is a letter that was sent by division management from Helena to the Board of Directors of the First National Bank

& Trust.
Q. And does this relate to your examination?
A. Yes.
Q. Does it summarize the conclusions and findings of the examination you conducted?
A. Yes. I read this document, and it does contain the essence of my examination.
Q. Were you the examiner in charge?
A. Yes, I was, yes.
Q. Now, what was the scope of your review

that you were -- that you conducted?
A. My purpose for being there and the scope of the inspection examination was to determine the safety and soundness of the bank; to look into its future prospects and to make certain assessments and determinations as to whether the bank qualified for chartering under the laws of the State of Montana.
Q. Just to make sure I didn't miss this, did you tell us when you were there?
A. May, I think it was the 24th, May 24th, during that week, of 1991.
Q. Thank you.
Now, what were the conclusions that you reached as a result of your examination and assessment?
A. My conclusions --
Q. And if you want to refer to the

letter --
A. Could I?
Q. Sure.
MR. SAVOY: Your Honor, I would just like to clarify.
Has this exhibit already been admitted into the record?

MR. TOWE: Yes.
THE WITNESS: I framed my conclusions around a fairly common skeleton of circumstances used by examiners in the state of Montana and in other examining agencies, and this is often characterized by something called a CAMEL analysis, including capital asset quality management earnings, liquidity and other features that I felt were unique and important to this examination.
My conclusions were that management had been effective in the control of bank operations; that asset quality -- and I'll be happy to expand on these points, but that asset quality was satisfactory, but that elements of it were marginally adequate, marginally satisfactory.
Capital was satisfactory when I arrived, and as I projected, some adjustments remained satisfactory.
Earnings appeared to be those of an ongoing, viable bank. I made certain projections for 1991 and for 1992 based on my

findings there.
And liquidity was above 50% at that

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time due to a portfolio of investments that included U.S. governments, agencies and high quality, such high quality bonds.

Q. (By Mr. Towe) And liquidity was adequate?

A. Yes.

Q. Almost too adequate?

A. Well, that's sometimes the problems with small banks.

MR. SAVOY: Objection, Your Honor, I think that we should at least constrain the examination to the document itself.

Clearly the witness has already added plenty of comments which don't appear in the Report of Examination, & it is wholly improper for counsel to even suggest that there are additional comments which are not in here.

MR. TOWE: Are you suggesting that I can't ask this witness what he did?

MR. SAVOY: I'm suggesting that you cannot testify for him, Counsel, thank you.

Q. (By Mr. Towe) With regard to the specific comments that are contained in the document, I want to call your attention to the first page and under the heading "Management",

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it is stated "Management is deemed effective".

And then there is a comment that deals with,

> "...the bank's having earned an adverse reputation in its relationship with present primary regulator".

What does that mean?

MR. SAVOY: I'm going to object, Your Honor. The document was created by Donald Hutchinson. There has not been any establishment that this witness himself wrote the statement,

> "...clouded somewhat by the bank's having earned an adverse reputation".

I think counsel needs to establish that before he asks this witness what it is that that statement means.

JUDGE SHIPE: Well, what is your objection?

MR. SAVOY: The objection is that he is unqualified to interpret a sentence in this examination letter. He did not write the

letter.

JUDGE SHIPE: Well, it is based -- the first paragraph states it is based on his

inspection, so I think we should see whether he knows anything about that subject.

Would you rephrase your question, Mr. Towe.

MR. TOWE: Okay.

Q. (By Mr. Towe) Calling your attention to the first sentence under the paragraph "Management", what is meant by the words

> "...bank's having earned an adverse reputation in its relationship with its present primary regulator"?

A. This examiner, in the course of preparing to go into the field out to Wibaux, and every examiner, to my knowledge, has a time that is called scoping. When you get ready to go into the field, then you learn, you get up and running in the condition or affairs of the banks as has been previously determined.

As part of the application process, I believe the bank had sent a copy of the OCC's examination of 1989 to the Commissioner, and

it had been passed on to me to read in getting ready for the exam in Wibaux.

From a reading of that 1989 examination, it was apparent that management did not enjoy a pleasant relationship with its present primary regulator. And that's undoubtedly what Mr. Hutchinson is referring

to also.
Q. Was that your observation?
A. That was my -- my assumption from reading that '89 exam.
Q. And that was the OCC exam?
A. Yes.
MR. TOWE: Could we get Exhibit 571, please.
(Discussion off the record.)
Q. (By Mr. Towe) Showing you what is Exhibit 573, is that the exam that you just referred to?
A. Yes, it appears to be.
Q. Now, did you, in connection with that exam, go through that carefully and do something with regard to the comments that were made in that exam?
A. Yes. Part of my process in scoping

and deciding what to do to make the qualifying and recommendations of the qualifications of the bank was not only to take a look at the existing CAMEL elements, but to also determine what, if any, findings had come from the previous regulator and what, if anything, had been done by bank management to address those findings, concerns, and so forth.
And what I did was, I took what I considered to be the major findings of this examination, and I put it on a work paper, and

I addressed them to see if anything had happened, yes or no.

The concerns primarily were, for example, a concern with the quality of investments and a booking there of losses. There were concerns about asset quality and the bookings of losses, and so forth, and other concerns.

And I just did a little work paper to see if something had happened, and some of them there had been changes, improvements, and so forth, and in others, there were no changes.

Q. Now, when you spoke of this scoping of the examination, and you indicated that's

fairly common among examiners generally, I think you indicated you have worked with at least three different government organizations examining financial institutions; is that right?

A. Yes, that's right.

Q. Now, can you tell me whether or not it -- sometimes a reputation such as you just described here follows a particular person or a management from bank -- from time -- examiner to examiner?

MR. SAVOY: Objection, Your Honor, calls for speculation.

Second of all, this witness was not being called as an expert witness to testify

with respect to the practice in the industry. It was my understanding that he was being called to discuss his findings in this Report of Examination.

If counsel has, I don't know whether it was his third, second, fifth amendment to the prehearing statement, you know, we can discuss what the scope of his testimony was supposed to be.

JUDGE SHIPE: I'll deny the objection. Let's move along.

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THE WITNESS: Would you rephrase the question.

(Whereupon, the record was read by the reporter.)

THE WITNESS: Yes, it has been my experience in the agencies within which I have worked that the scoping process, as you warm up to the examination, perhaps you have never been into the bank before, and you need to become familiar with certain matters unique to that bank, that does include access to any comments regarding the quality of management or their effectiveness. It certainly is not always the focus of a scope but should be included as a matter of general practice in the review of the examiner in charge and his supervisors before the exam begins.

Q. (By Mr. Towe) And does that follow from exam to exam?

A. It is very possible. Certainly an examiner who is not aware of previous reputations or management abilities would look to those for clues and for previous observations regarding management abilities and their cooperativeness in other matters.

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Q. Now, speaking of that, did you find Edward Towe cooperative when you were there?
A. During my on-site examination there, I found him to be cooperative and accessible.
Q. Did he ever withhold any information you requested?
A. To my knowledge, no.

UNITED STATES OF AMERICA - OFFICE OF THE TREASURER - OFFICE OF THE COMPTROLLER OF THE CURRENCY
IN THE MATTER OF TOWE
CAUSE NUMBERS OCC-AA-EC-93-42 & OCC-AA-EC-93-43
TR. OF PROCEEDINGS (VOL. XXXIV)
DATED AUGUST 18, 1995

Testimony of William Grant

the OCC --

JUDGE SHIPE: Well, I don't want to prolong this hearing. I won't rule on your motion to do so until I have heard Mr. Grant's testimony

MR. TOWE: May I proceed?

JUDGE SHIPE: Yes, you may, Mr. Towe.

MR. TOWE: We would recall Mr. Bill Grant.

WILLIAM GRANT,

having been previously sworn to state the truth, the whole truth, and nothing but the truth, testified further as follows:

JUDGE SHIPE: The witness has been sworn and remains under oath.

DIRECT EXAMINATION

BY MR. TOWE:

Q. Good morning.

A. Good morning.

Q. Are you the same William Grant that testified here earlier?
A. Yes, I am.
Q. And Mr. Grant, I have handed you a document which has been marked for identification as Exhibit R-239. Do you

recognize that document?
A. Yes, I do.
Q. Is this the document that you referred to when you testified earlier as some of your, or your report or notes from which the other document that you testified to was prepared?
A. Yes. I have reviewed the copy, the exhibit, and it is a copy of my field write-ups and report to Commissioner Hutchinson.
Q. And it does say to "Donald W. Hutchinson from William W. Grant"?
A. Yes.
Q. And is that you; is that correct?
A. Yes.
Q. And it contains your name on the last page?
A. Yes, it does.
MR. TOWE: I would move its admission into evidence.
MR. SAVOY: Your Honor, the OCC requests that if the Court should allow this exhibit to come into evidence, that it recognize the fact that the OCC may have to bring in

rebuttal witnesses to challenge his testimony.
JUDGE SHIPE: I'll receive the document

Well, that's who would have had the authority to make the decision.

Q. And to the best of your knowledge, that decision was made by the Commissioner or the Deputy Commissioner?

A. The supervisory authorities, I think, formally define -- are formally defined as the Commissioner, and he holds the title of Administrator, and perhaps Assistant Administrator.

In any case, that was where the decision would have been made.

JUDGE SHIPE: How much more examination do you have, Mr. Savoy?

MR. SAVOY: I believe I'm through, Your Honor. I just want to go through this one time.

(Pause.)

MR. SAVOY: No further questions, Your Honor.

JUDGE SHIPE: Redirect?

MR. TOWE: Yes, thank you.

REDIRECT EXAMINATION

BY MR. TOWE:

Q. I just want to ask you a couple of

things just to refer. If you would, please, on Page 5 to the Exhibit R-239, I believe counsel has already asked you about the first, or the second paragraph there. I want to ask you starting with the third paragraph.

"Although such actions may add to President Towe's reputation as being tough and contentious, most of what he did over the last four years with OCC was what any experienced capable CEO would have done to adequately protect the interest of his bank. To have accepted OCC's findings at face value could well have lost him his bank."

Is that a statement that you made, and is it accurate today?

A. Yes, that's correct.

Q. Calling your attention to the next page, on Page 6, at about the third paragraph up, the last sentence,

"Nevertheless, when the current state review is put side by side with the OCC's review..."; do you see that?

A. Yes, I see it.
Q. "... it is clear that the bases for the OCC's review have been at best significantly affected by the timing difference of the reviews and at worst show OCC's review to be unduly or unnecessarily harsh."
A. Yes.
Q. Is that your conclusion?
A. Yes.
Q. And is that accurate?
A. Yes, it is.
Q. Now, calling your attention over to Page 10, under "Former Examiner's Concerns", and I believe the second sentence on Page 10, where the starts out "However..."; do you see that?
A. Okay.
Q. "... in this instance and

with the benefit of 19 months of foresight that the OCC examiners did not have, the State's examiner does not generally concur with the OCC's position and findings of October 28,

1989. It is interesting to note that in the spring of 1988, an Administrative Law Judge separately arrived at similar conclusions regarding OCC's earlier positions after the judge was presented with related concerns in a hearing in Billings, Montana."

Q. Is that still accurate?

A. Yes, it is.

I believe that I was seeing a bank in different circumstances in May of 1991 than the OCC's examiner examined or saw in October '89.

Q. And if, in fact, the Administrative Law Judge had ruled at a hearing on some of the

issues, would it be appropriate for the OCC examiners to subsequently criticize that same issue?

A. Difficult question.

MR. SAVOY: Your Honor, I think there needs to be some clarification. I believe -- are we referring to the recommended decision of the ALJ prior to the time the Comptroller had issued his final decision?

MR. TOWE: Let me rephrase that question.

Q. (By Mr. Towe) If, in fact, subsequent to a hearing the Administrative Law Judge had made a recommendation with regard to certain items, would it be appropriate for the OCC to criticize those items without acknowledging that at least someone had ruled differently?

A. It would be appropriate to monitor the conditions upon which the judge had made his decision, that is to say, the conditions forward.

It would be inappropriate to take the same exact conditions and try to somehow recreate a supervisory circumstance.

Q. And would it be appropriate to send out

a letter such as the one you were asked about, R-111, seeking civil money penalties if that same issue had been ruled upon in a recommendation from the Administrative Law Judge and was currently pending before the Comptroller?

MR. SAVOY: Objection, Your Honor. It had not been ruled upon. It was merely a recommendation. Nothing was final until the Comptroller had issued his opinion.

JUDGE SHIPE: Well, the objection i denied.

Can you answer the question?

THE WITNESS: Yes.

If, in the case -- in the instance where a ruling had not been received, it would be appropriate under certain circumstances to use the supervisory tool.

However, if a ruling had already been made by the Administrative Judge, and that ruling had been passed on to the appropriate regulatory authority -- and incidentally, that's a material matter, the passing of the information down to the level where the examiner in the field goes out to the bank --

that examiner should have taken into consideration the rulings of the judge in his scoping of his examination, in his preparation for the examination.

It would not be inappropriate to monitor to make sure the ruling of the judge was being -- that the bank was still in accord with such rulings, however. That would be appropriate.

Q. (By Mr. Towe) All right.

Can I call your attention again back to the report, your report on Page 11, at the top of the page.

"This inspection revealed that OCC has clearly been a detractor of bank management as evidenced by the items cited above.

However, the survival of the bank today can be primarily traced to the bank's noncompliance and specific challenges directed toward the OCC."

Is that your statement?

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A. That is my statement.

Q. And do you stand behind that?

A. I do. I find it to be ironic; I find there to be some reconciliations between those -- in those words, but I do believe that's the case.

Q. And then about three paragraphs down, starting out with the paragraph "Large numbers of technical exceptions"; this is on Page 11 --

A. Mm-hmm.

Q. "Large numbers of technical exceptions identified during the loan review."

That refers to the '89 OCC exam; is that correct?

A. Yes.

Q. And,

"This inspection revealed only minimum technical exceptions to exist in the

loans reviewed."
Is that correct?
A. Yes.
Q. And going down to the violations of

law, is that your statement,
"No violations of law were noted during this inspection."
A. And that refers to Montana law.
Q. Surely. You were reviewing it for state compliance, okay.
A. Yes.
It would be better written, "no violations of Montana law were other than noted", yeah.
Q. And going down a couple lines later,
"The selling of adversely classified loans to affiliates was deemed to be legal and an appropriate option open to management."
Is that correct?
A. Yes.
Q. And further down it says,
"The inspection did not reveal any inappropriate insurance agency relationships."
A. That's correct. I am not -- I was not

aware of that. I subsequently became aware of something that has to do with the PMI issue, but I'm still not fully informed on that matter.

Q. PMI?

A. Some sort of private mortgage insurance --

Q. Oh, I see.

A. -- relationship.

Q. But aside from that, did you have any difficulty whatsoever with the insurance agency relationship?

A. No.

Q. And in the middle of the next paragraph, "The examiner is not aware that such liens -- referring to IRS liens -- constitute "crime against banking laws".

What was that quote from?

A. The Montana Code Annotated has a section in there that talks about crime against banking laws, and I believe that my notation, my annotations there, it could be contained in the 32-1-322, or it might be in 462; I would have to look that up.

Q. I believe you said on cross-examination that you thought the word "bias" was too strong,

but there was a predilection or presumption that was carried forward by the OCC. And did you

refer to that in a negative sense with regard to this bank and its management?

MR. SAVOY: Objection, Your Honor; leading the witness.

MR. TOWE: Oh, I'm, sorry.

Q. (By Mr. Towe) Can you please explain?

A. In the course of going from examination to examination, some supervisory agencies, the State of Montana, probably the OCC, sees its supervisory function to extend over not just one examining period, but over a continuum.

As part of that, the message of the condition of the bank, its management, its asset quality and so forth, are brought forth through the particular examiners who are assigned to do the examination.

It is brought forth in the -- by ways of planning, by examiner supervisors, and by the the scoping of the examiner in charge, we assume that the examiners in charge have some time to prepare to go out on an examination. To the extent that the message -- that the messages and the written material have been

written, and supervisory actions have been taken, this affects the new examiner that goes out there. He becomes aware of the condition and the issues and the supervisory concern levels accorded by his agency. He promptly becomes aware.

Q. And did that affect the subsequent examinations and the relationship between the management and the OCC?

MR. SAVOY: Objection, Your Honor. Calls for speculation.

JUDGE SHIPE: Denied.

THE WITNESS: It can affect -- it can affect the relationship between examiners and management.

Q. (By Mr. Towe) And do you have an opinion as to whether it did in this case?

A. I believe it did.

Q. Based on all the facts that you did review and in view of your review of state laws, did you find anything which would justify removal of Edward Towe or Thomas E. Towe for life?

MR. SAVOY: Objection, Your Honor. This is totally inappropriate. It is beyond the

scope of cross.

JUDGE SHIPE: I'll sustain the objection.

Q. (By Mr. Towe) Well, I believe you were asked about the civil money penalties on cross-examination.

Based on all the facts that you have reviewed, and in view of your review pursuant to state law, did you see any facts which would justify leveling civil money penalties against Edward Towe or Thomas Towe?

MR. SAVOY: Objection, Your Honor.

It is very clear that his examination was very limited in scope, and that was not the purpose of his examination. To attempt to garner any expert opinion from him with respect to whether CMPs are appropriate at this point in time is wholly inappropriate, and counsel shouldn't be allowed to do it.

JUDGE SHIPE: Well, the question is confined to what he saw.

You may answer.

THE WITNESS: I believe that the bank was making progress, certainly in part by the supervisory efforts of the OCC. We haven't

talked about the credit that supervisory agencies deserve in these matters.

But with the progress that was being made, it doesn't seem appropriate that civil money penalties would have been exacted. If - they may have been viewed as a potential if progress did not continue or in some fashion in that way, that is to say, the supervisory tool could have been unsheathed for the management to see.

But the exacting of civil money penalties, in my view, would not have been appropriate at this time.

MR. TOWE: Thank you. I have nothing further.